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ABSTRACT

This study probes the influences behind recent trends in State-local finance and attempts to ferret out the dominant influences that will prevail during the remainder of the seventies. It presents projections of State-local finance for fiscal years 1975 and 1980 that indicate general spending and revenues will grow at a pace that will tend to generate surpluses of some $13 billion in 1975 and $9 billion in 1980. The major element tending to mitigate the rise in spending is the expected leveling in enrollments in educational institutions and in the number of welfare recipients. The outlook for a somewhat higher rate of inflation in the seventies than in the sixties tends to narrow the full savings that might otherwise result. The publication suggests that the ability of States and localities to achieve a lasting state of financial balance is predicated on policy decisions on how potential surpluses will be used, future federal policy with respect to grant-in-aid programs, the manner in which the current controversy over local public school finance is resolved, and the willingness of State-local units to cut back from recent accelerated rates of expenditure growth to increases that are more in line with longer-term averages. (Author/DN)

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The Financial Outlook for State and Local Government to 1980

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Foreword

Six years ago a Tax Foundation study projected the outlook for state-local government finances in the decade ahead, under a carefully specified set of assumptions. The 1966 study, *Fiscal Outlook for State and Local Government to 1975*, accurately foresaw a number of developments which have since occurred. Yet in various respects, the course of events has veered from the path assumed, with the result that both revenue and expenditure levels are now running far higher than was suggested by developments up to the mid-1960's.

By their nature, projections are not predictions or forecasts. They can tell only what will happen under the assumptions specified. When the course of events departs significantly from earlier assumptions, the projected levels of activity become outdated, and it is time for a new assessment of the outlook.

This study, accordingly, is designed to revise the previous projections of state and local finance made for the year 1975, and to present new estimates extending to 1980. The background section (Chapter II) gives a capsule view of developments since 1965, the cutoff date for the previous study, and describes the approach and methodology, underlying assumptions, and general plan of this study.

Within the economic environment specified, the study estimates the levels of expenditure for each major state-local function which would prevail in 1975 and 1980 with real rates of increase per workload or population unit equal to those of the 1960's. The revenue potential from present sources and prospects for debt financing are next analyzed. Based on these magnitudes, and other claims on state-local funds, the study evaluates the prospective ability of state and local governments generally to meet their financial obligations during the 1970's.

Elsie M. Watters, Director of Studies, was primarily responsible for the research and preparation of this study.

The Tax Foundation is a private, nonprofit organization founded in 1937 to engage in non-partisan research and public education on the fiscal and management aspects of government. It serves as a national information agency for individuals and organizations concerned with government fiscal problems.

TAX FOUNDATION, INC.
October 1972

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I.

Summary and Conclusions

Long the leading "growth" sector of the economy, state–local government finance gained added momentum in the period from 1965 to 1970, as a new and higher growth rate was superimposed on the previous pattern. General spending rose from $75 billion in fiscal 1965 to $131 billion in 1970, or more than three-fourths. Annual rates of expansion, which had eased to 7½ percent in the first half of the sixties, jumped to an average of 12 percent in the last half and extended up to 13 and 14 percent in the most recent years reported, far exceeding increases in any other major sector of the economy.

The rise in expenditures was met in part from expanded revenues from existing sources, generated by economic growth and inflation, as well as through rapidly rising Federal grants. The added amounts from these sources, however, were insufficient to sustain the upsurge in spending. To make up the difference, state–local government units levied new taxes, raised the rates of taxes in effect, put higher price tags on services sold—almost doubling these nontax revenues—and borrowed amounts which increased their financial indebtedness by 44 percent.

As of mid-1972, state–local budgets generally were in a more comfortable financial position than had been experienced for many years. This condition resulted largely from extensive statutory tax increases in 1971, the accelerated pace of economic activity, and the sharp rise in Federal categorical grants in 1971 and 1972. There were also indications that the expansion in revenues was accompanied by some reduction in the rate of expenditure increase. Moreover, the states and localities, by the end of fiscal 1973, were still to receive some $8 billion in Federal grants under the revenue-sharing program enacted in late 1972.

This study probes the influences behind recent trends in state–local finance, and attempts to ferret out the dominant influences during the remainder of the seventies. Revised projections of state–local finance for fiscal year 1975 update those published by the Tax Foundation six years ago, and new projections are presented for 1980.

The findings of the study furnish grounds for cautious optimism concerning the state–local fiscal outlook. Under the conditions assumed, general spending and revenues would grow at a pace which would tend to generate surpluses of some $13 billion in 1975 and $9 billion in 1980.

The optimism springs from the indication that general revenues from the existing structure, without legislative changes in tax rates and with Federal aid programs as now legislated, would produce somewhat more than enough to provide real cost increases per service unit equal to those experienced during the sixties as a whole. The major element tending to mitigate the rise in

Table 1.1

State–Local General Expenditures

Actual and Projected, Fiscal Years 1960–1980

Function	Amount (billions)				Percent increase	
	Actual		Projected			
	1960	1970	1975	1980	1960–1970	1970–1980
Total	$51.9	$131.3	$214.8	$320.0	153	144
Education[a]	18.7	52.7	80.7	116.9	182	122
Local schools	15.2	37.5	55.5	78.9	147	111
Higher education	3.2	12.9	21.8	33.2	324	157
Highways	9.4	16.4	23.0	29.8	74	82
Public welfare[a]	4.4	14.7	27.1	39.5	233	169
Cash payments	3.3	7.4	13.4	19.7	123	167
Medical care	.5	5.0	10.0	14.2	923	182
Health and hospitals	3.8	9.7	17.6	29.9	155	209
All other	15.5	37.8	66.3	104.0	144	175

a. Includes items not shown separately.

Source: Actual data from U.S. Department of Commerce, Bureau of the Census; projections by Tax Foundation.

spending is the expected leveling in enrollments in educational institutions and in the number of welfare recipients. The outlook for a somewhat higher rate of inflation for the seventies than in the sixties as a whole, as incorporated in the projections, tends to narrow the full savings that might otherwise result.

Apart from the caveats implied in the study's assumptions, the ability of states and localities to achieve a lasting state of financial balance is predicated on: (1) policy decisions as to how potential surpluses will be used; (2) future Federal policy with respect to grant-in-aid programs; (3) the manner in which the current controversy over local public school finance is resolved; and (4) the willingness of state–local units to cut back from recent accelerated rates of expenditure growth to increases which are more in line with longer-term averages.

The fourth caveat deserves special emphasis. State–local spending in recent years has grown at rates (13 and 14 percent annually) which are not sustainable over an indefinite period without new legislative initiatives to enlarge the revenue base. There is of course nothing inexorable about the continuation of any particular historical spending pattern. However, in a rapidly rising sector of the economy, where aspirations seem persistently to reach new pinnacles, temptations to spend available funds will be powerful. To some extent dissatisfaction over high taxes may be offsetting. Perhaps the most realistic interpretation of this study's findings is not that surpluses will actually *occur*, but that the states and localities will have greater discretion in shaping tax, spending, and debt policies—more alternatives from which to choose—than in many years. One possibility is the rare option of tax rate reduction.

Expenditures

According to the projections, state-local general spending will rise from $131 billion in fiscal 1970 to $320 billion in 1980. (See Table 1.1.) The ten-year rise of 144 percent would be somewhat less than the 153 percent growth in the past decade. In terms of annual rates, the 1970–1980 rise is equivalent to 9.3 percent, compared to a 9.7 percent annual rate in the sixties as a whole. Higher rates, averaging 10 percent annually, are portrayed in the first half of the projection period, slowing to 8 percent in the latter half of the decade.

Education and welfare are the two most costly services, and together accounted for nearly three-fifths of the rise in total spending from 1965 to 1970. Slower growth in both of these categories is expected in the seventies. For all other services combined (i.e., the total less education and welfare), outlays are seen as rising at annual rates somewhat higher than in the decade of the sixties, reflecting differential rates of growth in prices. Among the major categories of expenditure, the greatest proportionate growth shows up in sanitation and sewerage, health and hospitals, welfare, interest on general debt, and the variety of functions grouped under "miscellaneous."

Spending would continue to rise at rates above population and income gains, with outlays per $1,000 of personal income growing from $169 in 1970 to $194 in 1980. In per capita terms, the rise is from $644 in 1970 to $1,386 in 1980, or 115 percent. The indicated per capita spending level in 1980 is almost five times the 1960 amount (Table 1.2).

Table 1.2
Per Capita Expenditures for Selected State-Local Functions
Actual and Projected, Fiscal Years 1960–1980

Function	Amount				Percent increase	
	Actual		Projected			
	1960	1970	1975	1980	1960–1970	1970–1980
Total general	$289	$644	$993	$1,386	123	115
Education	104	259	373	506	148	96
Highways	53	81	106	129	53	60
Public welfare	25	72	125	171	193	137
Health and hospitals	21	47	82	130	124	173
Police and fire	16	32	48	70	101	120
General control[a]	12	23	34	49	95	114
Interest on general debt	9	21	35	54	131	152
Sanitation and sewerage	10	17	40	49	74	193
Housing and urban renewal	5	10	17	25	119	141
Other general	35	82	133	203	133	147

a. Includes financial administration.
Source: Actual data from U.S. Department of Commerce, Bureau of the Census; projections by Tax Foundation.

Education

Forty cents of every dollar of state-local general outlays supports public education. The cost of education is estimated to increase from $53 billion in 1970 to $117 billion in 1980, or by 122 percent. This averages out at 8.3 percent annually, as compared to a rate of 10.9 percent in the period from 1960 through 1970. Local public schools will continue to account for over two-thirds of the total; however, greater proportionate increases are expected in colleges and universities. A relaxation in enrollment pressures is expected to exert a dampening influence on increases in both current and capital spending. Whereas local public school enrollments rose by 10 million (nearly one-third) during the sixties, they have already reached a plateau at around 46 million, where they are expected to remain throughout the seventies. While college enrollments will go up by about the same absolute number as in the past decade (260,000 additions a year), the percentage rate is less than half as much. Based on trends in the sixties, operating costs per student in local public schools would rise by over 8 percent annually, and those in higher education by 6 percent per year.

The slowing in enrollment growth of public schools and colleges alone will "save" states and localities close to $30 billion by 1980; i.e., spending would be $30 billion higher in that year if enrollments and per student costs were to grow as rapidly as in the 1960-1970 decade.

Local public school costs, despite the stationary enrollments, would more than double between 1970 and 1980, rising from $37 billion to $79 billion. The full study discusses possible developments, including changes in methods of financing, which would raise the projected spending levels.

In contrast to a more than quadrupling in outlays for higher education in the sixties, these costs are estimated to rise about 2½ times, from $13 billion in 1970 to $33 billion in 1980.

Public Welfare

Public welfare turned up the biggest surprises in recent years. Long the third-ranking state-local function in terms of dollar costs, welfare moved into second position—next to education—in 1971. In the first half of the sixties, welfare spending grew at 7½ percent annually; in the ensuing five years, at 18 percent a year. Unusually large increases continued into 1971 and 1972.

The number of welfare recipients rose from 7.8 million in 1965 to 13.8 million in 1970, and by June 1972 had reached 15 million, nearly 11 million of whom were in the aid for families with dependent children (AFDC) category. A number of socio-economic and program factors contributed to the sharp rise. Some grew out of the war on poverty, such as formation of community action groups to help the poor, the National Welfare Rights Organization, and the civil rights movement in general. All these factors contributed to a greater awareness by the poor of their legal right to public assistance. Court decisions, and state actions expanding programs to take advantage of matching Federal funds, were also contributing factors.

Recent trends suggest that many of these pressures influencing the growth in caseloads during the last half of the sixties may have spent their major force. In the 12 months ending June 1972, the increase in cash payment recipients was only 7 percent, in com-

parison with 21 percent in the preceding 12 months. Moreover, recent initiatives at both Federal and state levels will tend to restrain state–local outlays for money payments, medical services under Medicaid, and social services.

The burgeoning in AFDC caseloads was perhaps the most dramatic factor on the welfare scene in recent years, and accounted for 40 percent of the rise in welfare spending during the sixties. The increase in costs of medical assistance as a result of implementing the 1965 Federal law establishing Medicaid, however, represented 45 percent of the total increase.

The projections indicate total welfare outlays of $39 billion in 1980, more than 2½ times the 1970 amount of $15 billion, with the general expansion spread among cash living allowances, medical payments, and other services. The projected annual increase rate, 10 percent, compares with about 13 percent from 1960 to 1970, and with considerably higher rates in recent years.

Highways and Streets

The provision and maintenance of some 3.8 million miles of highways and streets represents the third ranking state–local service in terms of dollar costs. The highway share in state–local budgets declined markedly during the sixties and is expected to fall further during the seventies. The projections indicate an expenditure rise of 82 percent from 1970 to 1980, from $16 to $30 billion. The projected annual rate, 6.1 percent, is above that of the sixties, but significantly lower than for other major functions. Because of extremely large increases in highway construction and maintenance costs, the real volume of work has been, and is projected to be, virtually on a plateau. Capital outlays make up about two-thirds of highway outlays; maintenance expenditures, however, are increasing at a faster pace.

To some extent highway spending is restrained by existing financing arrangements, especially [illegible] for spending on projects with seemingly higher social priorities. A number of new Federal highway programs have opened up in recent years, and others can be expected as the 42,500-mile interstate system, four-fifths of which is open to traffic, nears completion (now scheduled for 1976). Although three-fourths of all roads and streets lie outside the Federal aid system, Federal policy will continue to exert a strong influence on state–local highway developments.

Health and Hospitals

Spending for health and hospitals, the fourth largest category, is projected to rise from less than $10 billion in 1970 to $30 billion in 1980, approximately tripling. The rate—12 percent annually—is higher than that of the sixties as a whole, and above that indicated for most other services.

State–local governments own and operate 2,257 hospitals, serving an average of 630,000 patients daily in 1970. The institutions provide care for 97 percent of patients in all psychiatric hospitals, about three-fourths of those in long-term general hospitals, and for over one-fifth of those in short-term general hospitals.

Recent trends, as incorporated in the projections, imply that state–local health and hospital services have held their share of the market among all public and private providers of such services and will continue to do so in the years ahead. In particular, the administrative role of state–local hospitals in the nation's total has been maintained, both

Table 1.3

State-Local General Revenue

Actual and Projected, Fiscal Years 1960–1980

Function	Amount (billions)				Percent increase	
	Actual		Projected			
	1960	1970	1975	1980	1960–1970	1970–1980
Total	$50.5	$130.8	$227.6	$329.0	159	152
State-local sources	43.5	108.9	179.2	262.1	150	141
Taxes	36.1	86.8	140.3	201.1	140	132
Current charges	5.3	14.9	25.7	39.5	180	166
Miscellaneous	2.1	7.2	13.2	21.5	245	197
Federal grants	7.0	21.9	48.4	67.0	213	206

Source: Actual data from U.S. Department of Commerce, Bureau of the Census; projections by Tax Foundation.

for general patients and those needing specialized treatment.

On the other hand, out-of-pocket costs to state and local treasuries have not risen as fast as outlays. These hospitals became more "self-supporting" during the sixties, as the share of current expenditures financed from fees and user charges rose from 27 percent in 1960 to 39 percent in 1970. Medicare and Medicaid appear to be largely responsible. These developments confirm indications six years ago to the effect that the financial responsibility of state–local units for health and hospitals might diminish with the introduction of new financing, but that the administrative role would generally be maintained or enlarged.

Other Expenditures

The four most costly functions discussed above make up about 70 percent of all state–local general spending. Outlays for the mixed category—"all other," including such services as police and fire, interest on debt, sanitation and sewerage and others—are projected to rise from $38 billion in 1970 to $104 billion by 1980, or 175 percent, at a rate somewhat higher than in the sixties generally.

Revenues

Significant changes in state–local revenue structures took place during the sixties. The most rapidly rising revenue source—in percentage terms—was state income taxation. State and Federal aid grew far more rapidly than receipts from local sources. As a result, the share of local governments in financing state–local programs dropped from 45 percent in 1960 to 39 percent in 1970. Revenues raised by localities in 1970 were about 13 percent ($8 billion) less than they would have been under the 1960 distribution of intergovernmental financial responsibilities.

Moreover, the performance of the property tax, beginning about the middle of the sixties, reflected these trends. In the postwar period up to 1960 the property tax provided between 46 and 48 percent of state–local taxes.

This share dropped to 44 percent by 1965 and further to 39 percent by 1970, the latest year reported. In terms of its contribution to total state–local general revenues from all sources, the decline was even more precipitous—property tax yields fell from about 33 percent of these revenues in 1960 to 26 percent in 1970.

Based on the 1970 structure, general revenues are projected as rising from $131 billion in 1970 to $329 billion by 1980, or about 2½ times, somewhat less than during the previous decade. (See Table 1.3.)

These are the amounts the present revenue system, without further tax-raising legislation or new Federal aid programs, would produce. If the present tax system were left to itself, total taxes would rise to around $201 billion by 1980, about 2.3 times their size in 1970. The outlook would be for a continuation of more intensive use of individual income taxes, stability in general sales tax shares, and further declines in the role of selective sales, property, and miscellaneous taxes. The property tax, although its role in the structure would continue to decline, as has been the pattern in recent years, would still be by far the largest single tax source, with yields of around $50 billion by 1975 and $70 billion by 1980.

Nontax revenues from state–local own sources are projected to grow from $22 billion in 1970 to $61 billion in 1980.

Federal grants-in-aid, $22 billion in fiscal 1970 (and an estimated $43 billion in fiscal 1973), are seen as rising to $67 billion by 1980. The projections assume the legislative extension of the recently enacted Federal revenue sharing program to 1980. For categorical aid programs, the projections imply that grants will grow commensurately with state–local expenditures for the associated programs. By 1980 Federal aid would account for 20 percent of state–local general revenues, up from 17 percent in 1970.

Over-All Finance

Under the conditions assumed, general revenues would exceed spending by around $13 billion in 1975 and by $9 billion in 1980, or by 6 percent and 3 percent, respectively. The margins are not large, but surpluses of even this magnitude would be unusual for the general accounts. These accounts are usually in a deficit position because of the long-standing tradition of financing sizable portions of capital outlay by borrowing, plus some use of short-term borrowing. Loan proceeds are not included in "revenue," and the retirement of debt issues does not enter as an "expenditure." The full study explores debt and other transactions and their relationship to the general accounts.

The study also examines forces influencing debt financing, and finds that growth in debt during the sixties was far less than in the previous decade and that outstanding debt rose much less rapidly than did revenues and expenditures. Total debt, around $70 billion in 1960, was equal to 1.48 times annual general revenues from state–local own sources; by 1970, while debt had risen to $144 billion, its ratio to own-source revenues had declined to 1.12. According to the projections, total debt would rise to $310 billion by 1980. (See Table 1.4.)

Annual long-term borrowing for new capital is projected to rise from $18

billion in 1970 to $26 billion in 1975 and $35 billion by 1980. Cash and security holdings of state–local units—exclusive of insurance trust systems for pensions and other purposes—are estimated to rise from $64 billion in 1970 to $145 billion in 1980. These represent funds held as offsets to long-term debt, funds from the sale of bonds held pending completion of construction, contingency reserves, and working capital.

Examination of the broader scope of state–local financial transactions leads to a narrowing of the potential surpluses as shown in the general accounts, but the difference rests mainly on somewhat arbitrary assumptions built into the model as to the amounts of borrowing, debt retirement, and additions to liquid assets. Actually state–local officials can exercise a considerable degree of discretion in such decisions. (See Table 1.5.)

Concluding Statement

Within the economic environment specified, this study has attempted to answer two basic questions: (1) What would the existing revenue structure yield in the seventies if left alone—that is, without new or higher legislative increases in taxes, with nontax sources following their past trends, and with Federal grants based on programs already in effect? and (2) What levels of expenditures could be expected with rates of improvements in state–local services per workload or population unit equal to those of the sixties as a whole?

It has been shown that, given the assumptions, the present revenue system, at existing tax rates, will produce about 2½ times as much in 1980 as in 1970. Growing expenditure requirements would pre-empt much of this growth. There would, however, within this framework of analysis, be a budget margin of some $13 billion—around 6

Table 1.4

Perspectives on State–Local Debt

Actual and Projected, Fiscal Years 1960–1980[a]

Fiscal year	Total debt outstanding (billions)	Debt as percent of	
		Own-source revenues	Personal income
Actual:			
1960	$ 70.0	148	17
1965	99.5	146	19
1970	143.6	124	18
Projected:			
1975	211.2	112	18
1980	310.0	113	19

a. Debt as of the end of the fiscal year.

Source: Actual data from U.S. Department of Commerce, Bureau of the Census; projections by Tax Foundation.

Table 1.5

Summary of Source and Use of Major State-Local Government Funds[a]

Actual and Projected, Fiscal Years 1965–1980
(Billions)

Source or use	Actual		Projected	
	1965	1970	1975	1980
Source of funds:				
General revenue	$74.0	$130.8	$227.6	$329.0
Profit on liquor stores	.3	.4	.5	.6
New long-term security issues	11.2	12.8	25.9	34.7
Other borrowing[b]	1.1	4.2	1.5	1.5
Total funds available	86.6	148.2	255.5	365.9
Use of funds:				
General expenditures	74.5	131.3	214.8	320.0
Long-term debt retired	5.0	7.0	10.0	15.0
Employee retirement	1.8	3.3	6.1	11.2
Deficit on utility operations	1.0	1.2	2.3	3.8
Additions to liquid assets	4.5	3.7	9.7	10.4
Total funds required	86.9	146.5	242.9	360.3
Funds available less funds required	−.3	+1.6	+12.6	+5.5

a. Excludes receipts, expenditures, and liquid assets of social insurance systems; utility and liquor store operations are entered on a net basis. Also excludes some interfund and other transactions not detailed separately in Bureau of the Census reports.

b. Net increase in total debt outstanding minus the difference between long-term debt issued and retired.

Source: Actual data from U.S. Department of Commerce, Bureau of the Census; projections by Tax Foundation.

percent—in 1975, with the percentage shrinking somewhat by the end of the decade. Experience with past budgets suggests that such margins are highly volatile.

Nevertheless, the projection results do not foretell broad general problems of fiscal crisis for state and local governments. Nor do they suggest a rosy financial future for each of the 71,000 or so taxing jurisdictions. There are needs not being met, and acute fiscal problems in some areas, particularly in some large and old cities. How to solve these "pocket" problems within our present intergovernmental revenue system, despite years of discussion, still remains something of an enigma.

Finally, the projections imply no value judgment as to how much of the nation's total resources should be channeled into the public sector, how much should be financed by each level of government, or the suitability of different tax sources in supporting government programs. Future decisions on these broad policy questions, as they evolve, will have an extremely important influence on the actual course of state-local finance in the seventies and beyond.

II.

Background and Assumptions

Six years ago, analysis of the financial outlook for states and localities led to the conclusion that, at least in the aggregate, these governments were better off than was generally realized. The projections were based on information available through fiscal year 1965 and on assumptions which seemed appropriate in the existing economic and social setting. Under the conditions specified, the conclusions were that existing revenue structures—without new or higher statutory rates of taxes, and with growth in Federal aids already legislated—could support expenditure increases averaging about 7 percent annually in the decade ending in 1975. Taking into account probable caseloads, costs, and prices, the study found that this rate of increase could take care of real improvement in over-all state-local services at the same rate as in the previous

Table 2.1

Comparison of 1965-Based Projections for State-Local Finance and Actual Results for Fiscal Year 1970

	General revenues			
	Own sources	Federal grants	Total	General expenditures
	Billions of dollars			
Projections:				
Original amounts[a]	88.3	20.3	108.6	105.9
Adjusted for "excess" price growth[b]	100.7	23.1	153.8	120.7
Actual	108.9	21.9	130.8	131.3
	Percent deviation, actual versus projections			
Actual compared to:				
Original projections[a]	+23.3	+7.9	+20.4	+24.0
Projections adjusted for "excess" price growth[b]	+8.1	−5.2	+5.7	+8.8

a. Original projections were presented in *Fiscal Outlook for State and Local Government to 1975*, Tax Foundation, New York, 1966.

b. The original projections assumed a general price rise of 1.6% per year, 1965 to 1970; the actual rise was 4.25% annually. Adjustment for this differential results in raising the 1965-based projections by 14% for 1970.

Table 2.2

Annual Rates of Change, Selected Price and Cost Measures

1960–1970
(Percent)

Series	1960–1965	1965–1970
Consumer price index	1.3	4.2
Medical care prices	2.5	6.2
Hospital daily service charges	6.2	13.4
Construction costs	2.7	6.6
Implicit price deflator—state-local purchases	3.1	6.0
Average annual employee salaries:		
State-local	4.3	7.0
Private industries	3.7	5.5

Source: Computed from data published by U.S. Department of Commerce.

decade, and—other financing considered—surpluses were a possibility in 1970 and 1975.

While the rate indicated was lower than the annual growth in outlays during the 1955–65 decade—somewhat over 8 percent—there were a number of signs suggesting a tempering of the future rate of increase. The potentially decelerating influences were primarily manifest in the changing population patterns that lay ahead, and the catching up that had been achieved on investment backlogs accumulated during the forties.

The 1965-Based Projections and Recent History

It scarcely needs saying that the course of events thus far has deviated substantially from the path indicated by the projections. In the first five years following the 1965 benchmark, general revenues grew not at the rate of 7 percent annually, but by 12.1 percent; at the same time spending rose by 12.0 percent a year. By *1968*, expenditures had almost reached the levels which had been projected for 1970; and by 1970, they were 24 percent above the amounts projected. Revenues were 20 percent higher (Table 2.1).

What caused these substantial differences? The major villain was inflation. The projections assumed moderate rates of general price increase, according to the trend of the first part of the sixties. The actual experience was that general prices went up three times as rapidly in the latter half of the sixties as in the first half. The "excess" rise in prices, as

compared to the assumed rate, accounted for a sizable portion of the [illegible] levels for fiscal 1970. Even with the adjustment for general prices, however, the 1970 outlays were nearly 9 percent higher than the projections, and revenues about 6 percent higher.

General price measures are not, of course, altogether suitable for adjusting public expenditures for price effects, because governments buy only limited quantities of the kinds of things that go into the market basket of the typical American family. There were similar "unanticipated" increments—above those in general prices—in state-local outlays for personal services, which make up about two-fifths of expenditures, as pressures were put on budgets to meet employee salary increases averaging 7 percent annually (compared to 5½ percent in the private sector). (See Table 2.2.) Prices paid for construction projects, hospital and health services, and still other items important in state-local budgets, advanced far more rapidly than did consumer prices generally. Reflecting these influences, the implicit price deflator for state-local purchases of goods and services rose at an annual rate of 6.0 percent from 1965 to 1970, nearly 2 percentage points in excess of the annual rise in consumer prices generally.[1]

Adding to these difficulties was the struggle of states and localities to finance their share of the explosive growth in welfare—both cash living allowances, and increases in the costs of new Medicaid programs far exceeding official estimates made when Federal enabling legislation was enacted in 1965. [illegible] as had been foreseen, placing restraints on expenditure growth in the latter part of the sixties. For example, the earlier decline in birth rates led to slackening in the rate of increase in public school enrollments and in other services for children. Growth in service requirements for the aged moderated, reflecting slower increases in the numbers in this age group as well as extended Federal social insurance coverage, including Medicare. But such retarding influences were more than offset by others working in the opposite direction.

Economic growth and inflation also had the effect of automatically generating additional revenues, but not to the extent of the expenditure increase. To meet the rise in spending, state-local general revenues were increased from $74 billion in 1965 to $131 billion in 1970 ($57 billion), or by over three-fourths (Table 2.3). Federal aids, rising rapidly in this period, provided $11 billion of the added revenues, but four-fifths of the increment came from state-local own sources, a great deal of it from tax-raising legislation. In addition, the states and localities almost doubled their revenues from charges and fees and miscellaneous sources from 1965 to 1970. Moreover, to pay for large capital outlays, not all of which are financed from general revenues, state-local units borrowed in amounts which brought their gross debt at the end of fiscal year 1970 to $144 billion, 44 percent higher than five years earlier.

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1. State-local expenditures, when adjusted for the rise in consumer prices, rose at an annual rate of 7.5 percent from 1965 to 1970, as compared to 5.7 percent annually when adjusted by the implicit price deflator. This deflator, prepared by the Bureau of Economic Analysis, U.S. Department of Commerce, is preferable to the consumer price index in some respects in translating current-dollar state-local expenditures into real terms. It has two distinct disadvantages, however: it treats increases in government employee compensation as price increases, allowing for no rise in productivity or quality; and it excludes transfer payments.

Table 2.2

Selected Measures of Change in State–Local Finance

Selected Fiscal Years, 1960–1970
(Dollar Figures in Billions)

Series	1960	1965	1970	Percent increase 1960–1965	1965–1970	1960–1970
Total expenditures	$61.0	$86.6	$148.1	42	71	143
General, total	51.9	74.5	131.3	44	76	153
Education	18.7	28.6	52.7	53	85	182
Public welfare	4.4	6.3	14.7	43	132	233
All other	28.8	39.7	63.9	38	61	122
Capital outlay	15.1	20.5	29.6	36	44	96
Current operations	45.9	66.0	118.4	44	79	158
Total revenues	$60.3	$87.8	$150.1	46	71	149
General, total	50.5	74.0	130.8	47	77	159
Own sources	43.5	63.0	108.9	45	73	150
Taxes	36.1	51.2	86.8	42	69	140
Other	7.4	11.7	22.1	58	88	198
Federal grants	7.0	11.0	21.9	58	98	213
Gross debt	$70.0	$99.5	$143.6	42	44	105
Wages and salaries	$25.2	$38.5	$66.5	53	73	164
Number of employees (thousands)[a]	5,530	6,849	8,501	24	24	54

a. Full-time equivalent basis.
Source: Basic data from U.S. Department of Commerce, Bureau of the Census, and Bureau of Economic Analysis. Computations by Tax Foundation.

Underlying Assumptions In This Study

Recent developments have heightened awareness of the fact that state–local finance is responsive to circumstances and events which also have an important impact on other sectors of the economy, including the individual business concern. These influences cover a broad range of natural, social, economic, and political elements—both domestic and international. Underlying the projections is the basic assumption that there will be no revolutionary change in any of these factors during the seventies. In particular, it is assumed that the extent of United States involvement in international military conflicts will be no greater than at present. Another caveat is that there will be no serious depression; the projections are consistent, however, with short-run cyclical swings such as those which have occurred since World War II.

Population. Population trends are important in appraising the outlook, as regards both growth in numbers and changes in characteristics such as age, regional location, urban–rural–suburban distribution, ethnic composition, and other attributes. Trends in most of these characteristics during the 1970's seem likely to follow along the patterns experienced in the past decade. Total

Table 2.4

Population of Selected Age Groups

Actual and Projected, 1960–1980[a]

Year	Total population	Elementary and secondary school age[b]	College age[c]	65 and over	21–64
	Number (thousands)				
Actual:					
1960	180,684	44,196	16,122	16,659	92,177
1965	194,592	50,002	20,202	18,162	96,696
1970	204,800	52,518	24,625	20,156	103,956
Projected:					
1975	217,375	49,969	27,714	21,859	112,658
1980	233,798	49,985	29,360	23,703	122,711
	Numerical change (thousands)				
1960–1970	24,116	8,322	8,503	3,497	11,779
1970–1980	28,998	−2,533	4,735	3,547	18,755
	Percentage change				
1960–1970	+13.3	+18.8	+52.7	+20.9	+12.8
1970–1980	+14.2	−4.8	+19.2	+17.6	+18.0

a. As of July 1.
b. Age 5–17.
c. Age 18–24.
Source: U.S. Department of Commerce, Bureau of the Census.

population is projected to rise from around 205 million in 1970 to 234 million in 1980, 1.3 percent annually, the same rate as in the past decade.[2] There will, however, be some significant changes in the age distribution with implications for state-local finance.

Projections for selected age groups in 1975 and 1980 are shown in Table 2.4. These estimates reflect the effect of declining birth rates, resulting in a reduction in the population of elementary and secondary school age, and a slackening of more than one-half in the rate of growth in the college-age group. The number 65 and over will continue to rise at rates above those of the population at large and at about the same rate as in the sixties.

One particular age characteristic merits mention because it affects potential economic output. That is the labor force age group. Whereas this group is defined technically as those aged 16 and over, most workers are from ages 21 through 64. Almost two-thirds of total population growth in the seventies will be in these age groups (21–64), as

2. See Appendix I for a range of alternative projections.

compared to less than one-half the population increase during the sixties.

General Economy. Present indications are that the labor force will rise from 86 million in 1970 to 101 million by 1980, or by 15 million persons. This represents an annual increment of 1.5 million, or 1.6 percent. (See Table 2.5.) Assuming productivity gains of 2.5 percent per worker,[3] gross national product, measured from 1969, would rise by 4.1 percent annually in constant dollars. The projections are also based on the assumption that general price inflation will gradually taper off from its recent high rates of over 5 percent to 3.5 percent annually by 1973 and will drop further to 3.0 percent in the latter half of the seventies.

If these assumptions materialize, gross national product in current dollars would rise from $929 billion in 1969 to $1.5 trillion in 1975 and $2.1 trillion by 1980. Measured from calendar year 1970, when the economy was in recession, the current-dollar projected rise for the decade is 120 percent, or slightly over 8 percent annually. It can also be assumed that changes in income distribution will continue to follow trends in the past decade, with larger and larger portions of all families shifting to higher income brackets and a decline in the portion with income below subsistence levels.

Methodology

In state-local governments decisions to spend are generally not made independently of revenue considerations. Most government units are required to have balanced budgets for current operating purposes, and restrictions are placed on the amounts which can be borrowed. This linkage between spending and taxing is most obvious in the case of the property tax, for which rates are set periodically in connection with consideration of local expenditure plans, e.g., in school districts. Similarly, the

3. This rate is for both the public and private sectors; for the private sector alone, the rate is somewhat higher, since government productivity is held constant in the national income accounts.

Table 2.5

Projections of Selected Economic Aggregates

1970–1980

Series	Actual 1970	Projected 1975	Projected 1980
Labor force (millions)	85.9	92.8	100.7
Gross national product (billions):			
Current dollars	$974	$1,510	$2,140
1969 dollars	923	1,183	1,446
Index numbers (1969 = 100):			
General prices	100.0	127.7	148.0
Productivity	100.0	116.0	131.2

Source: Actual data from Bureau of Labor Statistics, U.S. Department of Labor; and Bureau of Economic Analysis, U.S. Department of Commerce; projections by Tax Foundation.

governors present to state legislatures budgets incorporating an expenditure plan, along with a revenue plan, often including a request for new or increased taxes.

There can also be a reverse effect. Knowledge of the availability of a given sum in revenues, if it seems larger than anticipated expenditure, is likely to evoke pressures for spending the "surplus," given the apparently insatiable aspirations for more and better government services (and higher salaries) characteristic of the times.

The projections generally do not take into account the potential interdependence of revenue and expenditure decisions. Expenditures are projected for each major function separately without regard to the manner in which they are to be financed.[4] Wherever possible—mainly in education and public welfare—the method utilized is that of projecting caseloads, unit costs, and prices, based on legislative programs already in effect. However, an "improvement" factor per unit is added—equal to the real rate of change during the sixties as a whole. Thus to the extent that expenditure increases per caseload during the past decade were the result of legislative changes, similar effects are carried over into the projections.

For functions for which caseloads are not readily identifiable or subject to enumeration, outlays are projected on the assumption that real per capita increases will be equal to the rates experienced in the period from 1960 to 1970. It should be emphasized that the period of the sixties was not homogeneous. Whereas the first half was characterized by moderate increases in state–local expenditures, the rates of expansion accelerated markedly in the second half. The projections assume that these recently accelerated rates of change will moderate, yielding a trend pattern in between the extremes experienced in the two periods.

As for revenues, tax yields are projected on the basis of the 1970 tax structure, adjusted for new state tax enactments in 1971, but exclusive of any future new taxes or statutory increases in existing rates. Two categories of receipts do take account of expenditure trends: revenues from user charges and fees are estimated by linear extrapolation of recent trends in their relationship to expenditures by function; and the share of categorical Federal grants-in-aid is projected as rising commensurately with state–local expenditures for the associated functions, with some adjustments for Federal grants enacted recently.[5]

The outlook for debt financing is considered to be a function of projected levels of capital outlay. On the expenditure side, the projected levels of general spending are adjusted upward for additional financial requirements, such as increases in liquid assets commensurate with growth in debt and scale of operations.

Concepts and Definitions

Although the study draws on data prepared by various agencies, the concepts and definitions used in the projections are those of the Governments Division, Bureau of the Census, of the U.S. Department of Commerce. The Census classifications provide a framework for analysis and synthesis of major government functions into meaningful

4. See Appendix I for detailed methodology for each function.
5. In particular, allowance has been made for (a) general revenue sharing enacted in 1972 for a five-year period, with the projections assuming continuation of this program at a similar level through 1980; and (b) Federal grants under the "clean-water" bill approved in 1972.

totals. While some other agencies provide more abundant detail on their operations, comparable data are not available for all functions of government.

Throughout the study, principal emphasis is on the general government sector, which encompasses all government revenue and expenditure except that for utility, liquor store, and insurance trust amounts.[6] These latter activities are generally, though not always, self-supporting.

Content and Organization

Chapters III through VI deal with expenditures for the major functional groupings—education, welfare, health and hospitals, and highways. In Chapter VII a summary of expenditures is presented for all functions, along with per capita and related data. Revenue considerations constitute the subject of Chapter VIII. The final Chapter presents projections for other operations (non-general) which require partial support from general funds, and the outlook for over-all finance.

In treating each major subject, an attempt is made to define the concept of activity under consideration, to analyze historical trends with a view to identifying the underlying causal factors and gaining better perspective on future trends, and to present the assumptions behind the projections, along with the projections themselves. Background material of limited interest to the general reader, and detailed assumptions utilized in the study, are contained in the Appendix.

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6. The term utilities here relates only to water supply, electric power, gas supply, and transit systems owned and operated by local governments. Other commercial-type operations of government—port facilities, airports, housing projects, and toll agencies—are treated as part of the general government sector. *Governmental Finances in 1969–70*, Bureau of the Census, U.S. Department of Commerce, Washington, D.C., 1971, p. 1.

III.
Expenditures for Education

Forty cents out of every dollar of state–local general expenditure goes to support education. Among all levels of government, education outlays rank second only to those for national defense. More than 50 million students attend publicly controlled schools and colleges, nearly one out of every four members of the population at large, and instructional staffs number close to 3 million. Four-fifths of all educational expenditures are made by publicly controlled institutions.

State–local spending for education, $52.7 billion in fiscal 1970, was almost three times its level at the beginning of the decade, with the greatest acceleration occurring in the last five years. In recent years funds allocated to education have represented a stable portion of state–local budgets, but have grown consistently at rates above the rise in personal income and in population.[1]

Reports of problems and limitations in the educational system make frequent headlines, whereas achievements often go virtually unnoticed. Inputs do not necessarily correspond to outputs, but the figures demonstrate that efforts have been substantial. During the sixties, for example, public institutions awarded 23 million high school diplomas and a large share of the nearly 8 million college degrees earned. State–local institutions added over 850,000 persons to their instructional staff, and invested $70 billion[2] in educational buildings and other capital facilities. Among other influences, these developments contributed to rising educational levels in the population at large. For example, today nearly four out of five 18-year-olds are high-school graduates; ten years ago the portion was only two out of three. Moreover, for persons 25 years old and over, the median number of school years completed rose to 12.2 in 1970, as compared with 10.6 in 1960 (and 8.6 years in 1940).

The intergovernmental arrangements for financing and administering public education are shown in Table 3.1. Local schools administer (and disburse) about 70 percent of all educational outlays through funds provided in part by grants-in-aid from higher levels, primarily states. The states have principal responsibility for administering higher education, although their financial role in local school support is greater. From a budgetary standpoint, about 40 percent of state general expenditures go for education (direct and intergovernmental) and 47 percent of local funds. Although amounts have risen somewhat in recent years, Federal outlays for education make up only about 2 percent of Federal general spending.

1. The relationship of spending for specific functions to total budgets and to population and income is shown in Chapter VII. Data on enrollments and instructional staff as discussed here are based on material in *Digest of Educational Statistics* and related publications of the U.S. Department of Health, Education, and Welfare, Office of Education. Expenditure data are from the U.S. Department of Commerce, Bureau of the Census.
2. In dollars of 1969–70 purchasing power.

Local Schools

Local public schools enroll nearly 46 million students, nine out of ten of the combined total for public and private schools, and employ an instructional staff of 2.3 million (Table 3.2). In fiscal 1970 public school outlays totaled $37.5 billion, 2½ times their size ten years earlier.[3] This growth reflected an expansion of almost one-third in enrollments, a doubling of per student outlays for current operations, and a rise of three-fifths in capital outlays.

Until very recent years tremendous expansionary pressures have been exerted on public school finance—by sharp increases in the population of school age, although other cost factors have also risen. From 1950 to 1970—public school enrollments grew by 20 million, an average of 1 million per year. This was in sharp contrast to previous experience. At the turn of the century the nation's public schools enrolled around 15 million. The numbers rose gradually to 25 million by around 1930, and remained almost unchanged throughout the thirties and forties. Thus the numerical rise since 1950 has been twice the increase recorded during the entire first half of the twentieth century.[4]

Influences behind Recent Trends

The postwar upsurge in births, leading to a larger population of school age by the early fifties, was accompanied by other developments increasing public school enrollments. Except for some lessening in enrollment growth, the sixties generally witnessed a continuation of long-term trends. Increasingly larger portions of the school-age popula-

3. "Local schools" comprise all direct expenditure by local governments, regardless of the source of funds, for education other than for institutions of higher education. Direct spending by states for public schools is not included. Also excluded are local government contributions to teacher retirement systems, interest on school debt, and debt retirement. Current expenditures cover instruction—salaries, free textbooks, supplies, etc.; administration; plant operation and maintenance; and miscellaneous school services principally linked to attendance, pupil transportation, school lunches (on a gross basis), recreation, and others.
4. In relative terms the rise was 80 percent from 1950 to 1970, and 67 percent from 1900 to 1950.

Table 3.1

Expenditures for Public Education by Level of Government and Type of Institution

Fiscal Year 1970
(Millions)

Type	All governments	Level of government		
		Federal	State	Local
Total expenditures	(a)	$8,897	$30,865	$38,970
Intergovernmental	(a)	5,844	17,085	32
Direct	$55,771	3,053	13,780	38,938
Local schools	37,461	—	437	37,024
Higher education	12,924	—	11,011	1,914
Other	5,385	3,053	2,332	—

a. Entries not additive because of overlapping intergovernmental payments.
Source: U.S. Department of Commerce, Bureau of the Census.

Table 3.2

Selected Factors Affecting Local School Finance[a]

Selected Years, 1959–60 — 1969–70

Factor	1959–60	1964–65	1969–70	Percent increase: Period 1959–64	Percent increase: Period 1964–69	Percent increase: Annual rate 1959–64	Percent increase: Annual rate 1964–69
Enrollment and staff (thousands):							
Population, aged 5 to 17	43,209	49,661	52,841	14.9	6.4	2.8	1.2
Enrollment, private and public:							
Total	40,782	47,716	51,319	17.0	7.6	3.2	1.5
Private	5,600	6,300	5,700	12.5	−9.5	2.4	−2.0
Public	35,182	41,416	45,619	17.7	10.1	3.3	1.9
Elementary	26,911	30,025	32,597	11.6	8.6	2.2	1.7
Secondary	8,271	11,391	13,022	37.7	14.3	6.6	2.7
Public schools:							
Average daily attendance	32,477	38,600	42,283	18.9	9.5	3.5	1.8
Instructional staff, total	1,463	1,811	2,270	23.8	25.3	4.4	4.6
Classroom teachers, total	1,355	1,648	2,014	21.6	22.2	4.0	4.1
Elementary	832	940	1,108	13.0	17.9	2.5	3.3
Secondary	524	708	906	35.1	28.0	6.2	5.1
Other instructional staff	108	163	256	50.9	57.1	8.6	9.5
Expenditures:							
Total (thousands)	$15,166	$21,966	$37,461	44.8	70.5	7.7	11.3
Current (thousands)	12,263	18,679	32,803	52.3	75.6	8.8	11.9
Capital (thousands)	2,903	3,287	4,658	13.2	41.7	2.5	7.2
Current expenditures per student in average daily attendance	378	484	776	28.0	60.3	5.1	9.9

a. See also price and cost indexes in Table 2.3.

Source: Computed from data published by U.S. Department of Health, Education, and Welfare; and U.S. Department of Commerce, Bureau of the Census.

tion entered school, remained longer, and chose public rather than private schools. Today total school enrollment in all elementary and secondary schools equals 97 percent of the population in the ages from 5 through 17 years. Public schools absorbed 99 percent of the over-all rise in enrollments during the sixties, as the numbers in private schools increased less than 2 percent—

from 5.6 million in 1959 to 5.7 million in 1969.

Numerous influences other than enrollment growth have contributed to the rise in public school expenditures. Table 3.2 illustrates. The relatively greater increase in high-school level students than in elementary grades added to over-all pupil costs, both because of differentials in teachers' salaries and pupil–teacher ratios. In both elementary and secondary schools, the size of the instructional staff grew more than proportionately to the growth in students. In the period from 1965 to 1970 alone, 196,000 teachers were added to take care of enrollment increases, and another 170,000 to reduce pupil–teacher ratios. Thus pupil–teacher ratios in elementary schools declined successively from 28.7 in 1960 to 27.9 in 1965 and 24.8 in 1970. In high schools the ratio remained steady at 21.5 pupils per teacher from 1959 to 1965, but dropped to 20.0 in 1969–70. Generally rising prices meant higher expenses for such items as pupil transportation, library resources, textbooks, supplies, maintenance services and other goods and services purchased by local school systems.[5] Teachers' salaries, which make up three-fifths of current operating school costs, rose, on the average, by substantially more than did general prices.

This analysis highlights two points: in recent years, as well as in the decade ending in 1965, factors other than enrollments and general prices have accounted for the greatest part of the growth in school spending; and the force of these factors became especially pronounced during the latter part of the sixties. During the decade ending in 1965, increases in numbers of students accounted for about one-third of the constant-dollar rise in operating costs; in the following years, the importance of enrollment gains fell to 17 percent of the total rise. In this context the major measurable factor—claiming a large share of the total rise—was the increases in average teachers' salaries above the rise in consumer prices.

Trends in educational costs per student appear sensitive to rising incomes and standards of living generally. One measure of this effect is seen in the relationship of changes in current expenditures per student to per capita income. On the average during the sixties an increase of 1 percent in per capita income was associated with a rise of 1.25 percent in per pupil outlays for education; that is to say, per pupil spending rose at an annual rate exceeding by one-fourth the concurrent rate of rise in per capita income (both measured in dollars of current purchasing power). As a result, *per pupil* current expenditures rose from 17 percent of *per capita* personal income in 1960 to 20 percent in 1970.

Although capital outlays rose far less rapidly than those for current operations, the dollar levels of 1970 spending were three-fifths higher than ten years earlier. Modest year-to-year increases in the period up to 1965 were followed by much sharper gains in the latter part of the period. During the entire ten-year period, over 700,000 new school rooms were built at total costs, measured in 1969–70 dollars, of $46.3 billion.[6]

5. Numerous examples can be cited: e.g., in the decade ending in 1968 costs of transporting pupils at public expense increased 2½ times, reflecting the rise in enrollments, an increase in the portion of pupils being transported at public expense, and rising costs of operating buses; the average price of a hardcover book (excluding texts) rose by 77 percent; more expensive teaching equipment was introduced; more attention was devoted to handicapped or exceptional children.

6. *Projections of Educational Statistics to 1979–80*, U.S. Department of Health, Education, and Welfare, Office of Education, Washington, 1971, p. 96.

Did the availability of funds have pronounced effects on school outlays in the sixties? The answers are not clear. There has been no major shift in intergovernmental arrangements for public school finance since the late forties (Table 3.3). The local government share, coming largely from property taxes, accounts for about 56 percent of the total; the states through grants-in-aid pay 37 percent, and the remainder comes from the Federal government, largely under provisions of the Elementary and Secondary Education Act of 1965 (ESEA). According to U.S. Office of Education estimates, ESEA had the effect of raising current school spending in 1969–70 by $4.4 billion, or 15 percent above the level excluding the effects of that legislation. Among the effects of ESEA were the addition of some 200,000 classroom teachers in the past five years, principally serving to reduce pupil–teacher ratios in programs for the disadvantaged.[7]

As regards capital spending, the failure of numerous school bond issues to gain voter approval in recent years has been highly publicized. As Table 3.4 indicates, in 1969 and 1970, for the first time during the decade, less than one-half of the funds sought in bond electrons was approved. The trend of approval has been downward since 1965. Actual bond sales and school capital outlay do not appear, however, to have been influenced significantly by the results of bond elections. In the latest years reported, capital outlays have trended upward in relation to bond sales. Although the evidence is not conclusive, these trends cast some doubt on the notion that voter opposition has exerted strong influence in holding down school capital outlays.[8]

Table 3.3

Percentage Distribution of Local School Revenue Receipts by Source

Selected School Years, 1929–1970

School year[a]	Source of funds			
	Total	Local[b]	State	Federal
1929	100.0	82.7	16.9	.4
1939	100.0	68.0	30.3	1.8
1949	100.0	57.3	39.8	2.9
1959	100.0	56.5	39.1	4.4
1967	100.0	54.4	36.6	9.0
1968	100.0	55.2	36.7	8.1
1969	100.0	55.8	36.9	7.3
1970	100.0	55.5	37.0	7.5

a. Represents beginning date of school year.
b. Includes other sources.
Source: U.S. Department of Health, Education, and Welfare, Office of Education.

Factors Affecting the Outlook

Local public school finance in the seventies will be determined by enrollment patterns, and perhaps to a greater extent, as was true in the sixties, by a host of economic and policy variables influencing costs per pupil in attendance.

Enrollments. During the seventies, for the first time in three decades, it now appears that pressures on public school resources resulting from enrollment gains alone will be nil. While some uncertainties exist, the outlook is gen-

7. *Ibid.*, pp. 53, 93.
8. Several limitations apply to judgments in this area: (a) not all bonds are subject to voter approval; (b) voter approval and actual sales of bonds do not necessarily occur within the same fiscal year; and (c) there is no way of knowing how much larger capital outlays would have been in the absence of voter reactions. The relationship between bond sales and capital outlay is discussed in Section IX.

erally for a period of stability, with enrollment levels remaining on a plateau at around 46 million (Table 3.5). There will be growth in secondary schools, offset by declines in elementary schools.

The zero-rate growth in the decade ahead results from an expected decline of 5 percent in the population of school age (5 to 17 years), attributable to the lowering of birth rates in the sixties. Partly offsetting are two factors: (1) continued shifts in the portion of students going to public as compared to private schools and (2) the tendency of increasingly larger portions to remain in school until they receive high school diplomas.

It should be noted that these projections depend in part on assumptions about future fertility rates as well as shifts from private to public schools. Thus they are subject to some error.

Within the range of assumptions now generally accepted, however, the margin of error resulting from fertility assumptions appears relatively small. The choice of assumptions will not affect the 1975 projections, since children who will be in school then are already born. By the 1979–80 school year, the projections for kindergarten and the first four grades do depend upon the course of future birth rates, and total enrollments could vary within a relatively narrow range.[9]

After rising slowly in the early sixties, private school enrollments

9. See *Current Population Reports*, series P-25, No. 470 (November 1971), U.S. Department of Commerce, Bureau of the Census.

Table 3.4

Public School Bond Elections and Related Factors[a]

Fiscal Years 1960–1970

Fiscal year	Bond elections			Exhibit	
	Par value (millions)		Percent of bonds passed (by value)	Bond sales	Capital outlay as percent of bond sales
	Total	Passed			
1960	$2,672	$1,792	67.1	$2,198	128
1961	1,605	1,218	75.9	2,357	122
1962	1,849	1,273	68.9	2,568	116
1963	2,659	1,851	69.6	2,274	119
1964	2,672	1,900	71.1	2,570	122
1965	3,129	2,485	79.4	2,823	131
1966	3,560	2,652	74.5	2,883	130
1967	3,063	2,119	69.2	3,254	123
1968	3,740	2,338	62.5	2,917	146
1969	3,913	1,707	43.6	2,904	160
1970	3,300	1,600	49.5	2,813	181

a. Not all bond issues require voter approval.
Source: U.S. Department of Health, Education, and Welfare, Office of Education.

Table 3.5

Enrollments and Attendance in Public Elementary and Secondary Schools[a]

Actual and Projected, Selected School Years, 1954–1979

School year[b]	Enrollments			Average daily attendance
	Total	Elementary	Secondary	
	Number (thousands)			
Actual:				
1954	29,549	23,106	6,443	26,978
1959	35,182	26,911	8,271	32,477
1964	41,416	30,025	11,391	38,600
1969	45,619	32,597	13,022	42,283
Projected:				
1974	45,800	30,900	14,900	42,400
1979	45,600	30,600	15,000	42,200
	Numerical change, 5-year intervals (thousands)			
1954–59	5,633	3,805	1,828	5,499
1959–64	6,234	3,114	3,120	6,123
1964–69	4,203	2,572	1,631	3,683
1969–74	181	−1,697	1,878	117
1974–79	− 200	− 300	100	− 200
	Percentage change, 5-year intervals			
1954–59	19.1	16.5	28.4	20.4
1959–64	17.7	11.6	37.7	18.9
1964–69	10.1	8.6	14.3	9.5
1969–74	.4	− 5.2	14.4	.3
1974–79	− .4	− 1.0	.7	− .5

a. Regular day schools only.
b. Represents beginning date of school year.
Source: Actual data and projections from U.S. Department of Health, Education, and Welfare, Office of Education. Computations by Tax Foundation.

reached a peak of 6.3 million in the years from 1963 through 1966. Since then the trend has been downward, with enrollments dropping by 400,000 (about 10 percent) by the 1969–70 school year. The projections incorporate a further decline of 300,000 students by 1972, with the level remaining stationary at 5.4 million throughout the remainder of the seventies. Severe deterioration in the financial status of private schools, leading to massive school closings, could of course serve to displace even more pupils from private schools and to add correspondingly more to local public school systems.[10]

10. Appeals of parochial and other nonpublic schools for government financial support from state and Federal sources have thus far met with little success. Loosening of restrictions against such aid could, of course, serve to maintain levels of nonpublic enrollments, with the effect for public coffers showing up in aid to nonpublic schools rather than in the form of enrollment changes.

Also of potential—though lesser—influence on enrollments are future trends in nursery school attendance, primarily in the 3- and 4-year age group.[11] Altogether, some 1.1 million children attend public and private nursery schools. The number more than doubled from 1965 to 1970, in spite of a decline in the population in the corresponding age groups. The number enrolled in Head Start and similar programs sponsored by public agencies increased from 127,000 to 333,000 in the five-year period, or 162 percent. Private prekindergarten enrollments, however, still outnumber public enrollments by more than two to one. The number of 3- and 4-year olds will rise from 8 million in 1970 to within a range of 8 and 10 million in 1980.[12]

Despite the foregoing uncertainties, it would appear, on balance, that the enrollment projections are generally accurate within a relatively narrow band for error, and that enrollment trends can be expected to have a moderating influence on future spending for local public schools.

Per Pupil Expenditures. Apart from enrollments, there are a number of proposals under discussion which, if approved, would tend to cause spending per pupil to rise above rates of the sixties. A full discussion lies beyond the scope here, and no estimates of financial effects are attempted. At least three deserve mention, however: (1) recommendations for more attention to education of the disadvantaged, particularly preschool ages in urban areas;[13] (2) proposals for greater attention to the needs of an estimated 2 million "gifted and talented" students in secondary schools who can benefit from educational programs or services other than those provided by the regular school programs;[14] and (3) numerous different proposals for revisions in intergovernmental arrangements for public school finance. To some degree the trends in per student costs during the sixties reflect improvements in educational opportunities for special groups, such as the disadvantaged and the gifted. The projections allow for similar effects in the seventies. Undoubtedly the largest questions in future educational finance appear to turn on the means of financing public schools.

For some years proposals have been advanced for shifting a greater share of the tax burden for public school finance to higher levels of government, and away from the local property tax. Suggestions have taken various forms. Some would abandon the local property tax completely as a source of school support; others take the form of attempting to improve state–local intergovernmental aid formulas to remove inter-area disparities in per student educational resources, placing less over-all reliance on the property tax. Again, some groups advocate virtually complete state take-

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11. Data in this paragraph on enrollments are based on the October 1970 survey of "School Enrollment in the United States: 1970," *Current Population Reports*, Series P-20, U.S. Department of Commerce, Bureau of the Census, March 5, 1971.
12. *Current Population Reports*, Series P-25, *op. cit.*
13. See, for example, *Education for the Urban Disadvantaged: from Preschool to Employment*, A Statement on National Policy by the Research and Policy Committee of the Committee for Economic Development, New York, New York, 1971.
14. In November, 1971, the U.S. Commissioner of Education released a report on the education of gifted and talented youth based on a study required by Congressional mandate under the Elementary and Secondary Education Amendments of 1969. Among other findings, the report noted that education for such children rates a very low priority at the Federal, state, and most local levels. *H.E.W. News*, Press Release, Office of Education, Washington, D.C., November 22, 1971.

over of public school costs,[15] and others see massive increases in Federal grants as the solution to problems in financing the schools.

Recent judicial decisions challenging present methods of school finance lend new currency to issues in school finance, by questioning the constitutionality of the local property tax as now levied for the support of local schools.[16] A full discussion lies beyond the scope of this study. At heart of the issue is the fact that property tax collections, which financed some $18 billion of local school outlays in 1970, produce wide disparities among school districts in per pupil resources, thus leading to unequal educational opportunities. The U.S. Supreme Court will rule on an appeal from the Texas case in the session beginning in October, 1972.[17] Early in 1972 President Nixon asked the Advisory Commission on Intergovernmental Relations to study the value-added tax as a possible means for financing an expanded Federal share of educational costs and at the same time achieving other tax reforms. The Commission's report is expected in late 1972.

Whatever the outcome of these pending questions in Federal policy, recent recommendations in the states suggest an expanded role of the states in public school finance and the evening-out of per pupil spending disparities among school jurisdictions. Widespread approval of such proposals could be expected to raise school spending above the levels it would otherwise reach, for two reasons: (1) It is axiomatic that raising per pupil spending in the poorer districts to amounts prevailing in the average or above-average districts will increase total spending (there have been few suggestions that spending would be reduced in the more wealthy districts). (2) Moreover, research suggests that the mere process of shifting financing to higher levels tends to lead to higher costs than would otherwise prevail. In particular, increases in the portion of school costs borne by the state, unless accompanied by offsetting restrictions on local taxing powers, can generally be expected to result in higher levels of combined state-local spending. These effects would result from the higher elasticity of state taxes and the broadening of the total tax base, as well as through lessening restraints on growth which might otherwise be exercised by local opposition to property tax increases.[18]

Projections—Local Schools

While uncertainties exist on all sides, it is probably safer to make stronger assertions concerning the likelihood of relative stability of future enrollments than about future expenditures. The

15. As early as 1969, for example, the Advisory Committee on Intergovernmental Relations recommended state assumption of "substantially all" responsibility for financing public school education (*State Aid to Local Governments*). Recently several state commissions and two Federally financed groups have made similar proposals: The President's Commission on School Finance (*Schools, People & Money—The Need for Educational Reform*, 1972) and National Education Finance Project headed by Roe L. Johns of the University of Florida (*Future Directions for School Financing . . .*, 1971).

16. The first of these was *Serrano v. Priest*, August 30, 1971, California Supreme Court. Others followed in Minnesota, Texas, New Jersey, and Arizona. For a summary of the background, see David H. Kurtzman, "The Courts Look at Educational Equality," *Tax Review*, Tax Foundation, June 1972. Other references to current discussions appear in *Public School Finance*, Research Bibliography No. 49, Tax Foundation, July 1972.

17. In *Rodriguez et al. v. San Antonio Independent School District*, a three-judge U.S. District Court ruled that the present method of financing Texas public schools is in violation of both the United States and Texas constitutions and ordered the legislature to work out new financial arrangements. U.S. District Court, Western District of Texas, San Antonio Division, Civil Action No. 68–175–SA, December 23, 1971.

18. For discussion of the effect of different state-aid formulas on local school spending, see H. Thomas James and others, *Wealth, Expenditure and Decision-Making for Education*, School of Education, Stanford University, Stanford, California, 1963, p. 34 ff., and Jerry Miner, *Social and Economic Factors in Spending for Public Education*, Syracuse University Press, Syracuse, 1963, p. 85.

projections appear in Tables 3.6 and 3.7.

Operating Costs. For operating costs per pupil, the projections incorporate the pattern of increase experienced during the sixties. From 1960 to 1970, average outlays per student more than doubled, rising from $370 to $776, an average annual rate of 7.4 percent. Adjusted for the rise in general prices, the increase was 4.7 percent per year. Since it is assumed that prices for the seventies as a whole will go up somewhat more rapidly than in the sixties, the projected rate of increase in per student outlays from 1970 to 1980 rises to 8.2 percent. Thus per student costs would go up about 120 percent, to a level of $1,706 by 1980. This rate of change, approaching 5 percent per student in real terms, would raise current local school costs by $40 billion between 1970 and 1980, in dollars of current purchasing power. Per pupil outlays would rise from the present 20 percent of per capita income to around 24 percent—or, as in the sixties, at a marginal rate exceeding the per capita income rise by one-fourth.

Capital Outlays. Notwithstanding the leveling in enrollments, construction of new schoolrooms can be expected to

Table 3.6

Expenditures for Local Public Schools by Object

Actual and Projected, Selected Fiscal Years, 1955–1980

Fiscal year	Total local schools	Current operations		Capital outlay
		Total current	Average per pupil	
	Amount (millions)			
Actual:				
1955	$10,129	$ 7,390	$ 274	$2,739
1960	15,166	12,263	378	2,903
1965	21,966	18,679	484	3,287
1970	37,461	32,803	776	4,658
Projected:				
1975	55,466	49,862	1,176	5,604
1980	78,875	71,993	1,706	6,882
	Percent increase, selected intervals			
1955–60	50	66	38	6
1960–65	45	53	28	13
1965–70	71	76	55	42
1970–75	48	52	52	20
1975–80	42	44	45	23
1960–70	147	167	105	60
1970–80	1[illegible]	119	120	48

Source: Basic data from U.S. Department of Commerce, Bureau of the Census. Computations and projections by Tax Foundation.

continue in order to serve needs created by such factors as migration, obsolescence, destruction by fire and urban development, and school reorganization and consolidation. The projections foresee an extension of trends in the sixties, with the construction of 700,000 new classrooms during the decade, at total costs (1969–70 dollars) of $49 billion, about six percent more than in the sixties as a whole.[19] (See Table 3.7.) When allowance is made for increases in construction costs, annual expenditure levels would rise from $4.7 billion in fiscal 1970 to $6.9 billion in 1980, or 48 percent.

Over-All Expenditures. These components add up to total projected public school outlays of $55.5 billion in 1975 and $78.9 billion in 1980, in comparison with the $37.5 billion expended in 1970. For the decade as a whole, the indicated annual rate of increase is 7.7 percent, as compared to 9.5 percent during the sixties as a whole, and with 11.3 percent during the last half of the sixties. The differential rate of growth is largely accounted for by the outlook for stability in enrollments, and the resulting effects on both current and capital costs.

Higher Education

About two-fifths of the nation's 2,525 institutions of higher education are operated by state and local governments. These institutions enroll around 5 million students, about 70 percent of the combined total in public and private colleges, and engage professional staffs of close to 600,000 persons. Among the public institutions, the majority—634—are two-year colleges; the 426 four-year institutions, however, account for over three-fourths of total enrollments.[20]

Measures of higher education expenditures vary widely according to how "higher education" is defined. Various concepts are reported by different agencies, resulting sometimes in wide disparities in stated amounts of spending. The reasons have to do largely with disparate functions performed by colleges and universities. In addition to instructing students beyond the high-school level, these institutions carry on numerous other activities, such as operating hospitals, experimental farms, laboratory schools, cafeterias, sports events, book stores, and research; and providing financial aid to students.

The definition adopted here, as in the rest of this study, is that of the Bureau of the Census. Under this concept, revenue and expenditure for dormitories, athletic events, and other auxiliary services are on a gross basis. (On the whole, these activities are more than self-supporting.) The Census definition excludes from "higher education" the following: agricultural experiment stations and extension services (classed under natural resources); university-operated hospitals serving the public (classed under hospitals); and state supervision of schools and colleges, state tuition grants, and fellowships (all classed under "other education").

Influences behind Recent Trends

Expenditures for higher education more than quadrupled in the sixties, rising from $3.2 billion in 1960 to $12.9 billion in 1970. As in other activities, expansion in the latter half of the sixties

19. See Appendix I for the derivation. The basic projections are those of the U.S. Office of Education.
20. *Digest of Educational Statistics*, 1970, U.S. Department of Health, Education, and Welfare, Office of Education, and related reports.

was markedly greater than in the first half. Table 3.8 illustrates some of the underlying influences.

The sheer crunch of growing enrollments has been the most obvious factor in the rise in higher education costs. This trend stemmed in part from the fact that persons of college age became more numerous, increasing at the rate of 4.4 percent annually, nearly four times the rate of the total population. These effects were accentuated by the continuation of other trends, resulting in a rising portion of high-school graduates entering college (now 60 percent as compared to 52 percent a decade ago). For public institutions, these influences were compounded by the tendency of an increasingly larger portion of students to enter publicly controlled colleges, as opposed to private. This development was especially pronounced in the latter part of the sixties, when enrollment in private institutions grew by less than 3 percent annually, whereas attendance at public institutions rose by 11 percent per year. During the sixties as a whole, public colleges and universities absorbed 85 percent of the growth in enrollments, an increase for these institutions of 3.7 million students (full and part-time), or 175 percent.

Unlike the trend in local public schools, additions to college instructional staffs tended to rise slightly less rapidly than enrollments. Other influences on outlays—average salaries, general prices, construction costs—had results comparable to those described above for local schools.

The rise in enrollments alone appears to have explained more of the increase in expenditures in colleges and universities than in the local public schools, particularly in recent years. Average current expenditures per student in colleges increased at the rate of 6.7 percent annually from 1965 to 1970, or by 2.5 percent when adjusted for general price changes. In local schools, the per student cost increase, measured in real terms, was 5.7 percent. The most apparent explanation of this differential is that a considerable portion of the teachers added served to reduce the ratio of pupils to teachers, whereas in the colleges, these ratios appear to have remained relatively unchanged.[21] Another factor of influence was the changing mix of college students as

Table 3.7

Construction of Public Elementary and Secondary School Classrooms and Capital Outlay

Actual and Projected for Five-Year Periods, School Years 1955–1979

School year[a]	Class rooms completed (thousands)	Capital outlay in 1969–70 dollars[b]	
		Total (millions)	Per room
Actual:			
1955–59	343	$20,900	$60,900
1960–64	344	21,600	62,800
1965–69	359	24,700	68,900
Projected:			
1970–74	350	24,500	70,000
1975–79	350	24,500	70,000

a. Represents beginning data of school year.
b. Adjusted by Associated General Contractors construction cost index.
Source: U.S. Department of Health, Education and Welfare, Office of Education.

21. For a discussion of other factors, including the effects of student unrest, tending to hold down public appropriations, see The Carnegie Commission on Higher Education, *The More Effective Use of Resources—An Imperative for Higher Education*, McGraw-Hill, New York, 1972, pp. 28–29.

Table 3.8

Selected Factors Affecting Higher Education Finance[a]

Selected Years, 1959–60 — 1969–70

Factor	1959–60	1964–65	1969–70	Percent increase: Period 1959–64	Period 1964–69	Annual rate 1959–64	Annual rate 1964–69
Enrollment and staff (thousands):							
Population aged 18–21	9,280	11,519	14,236	24.1	23.6	4.4	4.3
Enrollment, private and public, total	3,571	5,280	7,917	47.9	49.9	8.1	8.4
Private	1,438	1,812	2,078	26.0	14.7	4.7	2.8
Public	2,134	3,468	5,840	62.5	68.4	10.2	11.0
Public institutions:							
Degree-credit enrollment, total	1,984	3,180	5,260	60.3	65.4	9.9	10.6
4-year	1,628	2,559	3,965	57.2	54.9	9.5	9.2
2-year	356	621	1,294	74.4	108.4	11.8	15.8
Full-time equivalent	1,648	2,671	4,536	62.1	69.8	10.1	11.2
Professional staff positions, total[b]	230	353	589	53.5	66.9	9.0	10.8
Instructional staff	189	283	479	49.7	69.3	8.4	11.1
Other positions[c]	40	70	110	75.0	57.1	11.8	9.5
Expenditures:							
Total (thousands)	$3,202	$5,863	$12,924	83.1	120.4	12.9	17.1
Current (thousands)	2,443	4,418	10,219	80.8	131.3	12.6	18.3
Capital (thousands)	759	1,445	2,705	90.4	87.2	13.7	13.4
Current expenditures per student[d]	1,564	1,764	2,444	12.8	38.5	2.4	6.7
Average charges per student[e]:							
Tuition, board and room, total	$822	$950	$1,198	15.6	26.1	3.0	4.8
Tuition and required fees	202	243	320	20.3	31.7	3.8	5.7
Board[f]	413	436	511	5.6	17.2	1.1	3.2
Dormitory rooms	207	271	367	30.9	35.4	5.5	6.3

a. See also price and cost indexes, Table 2.3.
b. Includes full-time and part time professional positions in 4-year and 2-year institutions of higher education.
c. Includes administration and services, and organized research.
d. Per full-time equivalent degree-credit student.
e. Per full-time undergraduate resident degree-credit student.
f. 7-day basis.

Source: Actual data from U.S. Department of Health, Education, and Welfare, and U.S. Department of Commerce; computations by Tax Foundation.

Table 3.9

Total and Full-Time Enrollments in Public Institutions of Higher Education, by Institutional Type[a]

Actual and Projected, Selected School Years, 1954–1979

School year[b]	Enrollments			Total, full-time equivalent
	Total	Four-year	Two-year	
	Number (thousands)			
Actual:				
1954	1,359	—	—	1,306
1959	1,984	1,628	356	1,562
1964	3,180	2,559	621	2,504
1969	5,260	3,965	1,294	4,181
Projected:				
1974	7,023	5,235	1,788	5,542
1979	8,671	6,409	2,262	6,798
	Numerical increase, 5-year intervals (thousands)			
1954–1959	625	—	—	256
1959–1964	1,196	931	265	942
1964–1969	2,080	1,406	673	1,677
1969–1974	1,763	1,270	494	1,361
1974–1979	1,648	1,174	474	1,256
	Percent increase, 5-year intervals			
1954–1959	46	—	—	20
1959–1964	60	57	74	60
1964–1969	65	55	108	67
1969–1974	34	32	38	33
1974–1979	23	22	27	23

a. Degree-credit students.
b. Represents beginning date of school year.
Source: U.S. Department of Health, Education, and Welfare, Office of Education; and Tax Foundation computations.

between two-year institutions, where costs are lower, and the four-year institutions. Still another yardstick of this difference lies in the comparison with personal income. While per pupil local public school current spending increased during the sixties at a rate one-fourth in excess of the rise in per capita personal incomes, spending per full-time college student rose at a rate one-tenth lower than the rate of rise in personal income.

During the last half of the sixties capital outlays for higher education totaled $12.8 billion in current dollars, nearly twice the $6.7 billion spent in the preceding five years. With adjustment for construction cost increases, the increase was, however, less than three-

fifths. Since 1966 capital outlays have been relatively stable at close to $2.6 billion annually in current dollars, and have actually declined when measured in dollars of constant purchasing power.

Outlook for College Enrollments

Enrollment projections of the U.S. Office of Education, as incorporated in this study, appear in Table 3.9. On a full-time equivalent basis, the number of students is estimated to rise from 4.2 million in 1969–70 to 6.8 million by 1979–80. The projected rate of increase for the coming decade is 63 percent, far below the 168 percent absorbed during the past decade. The numerical change, however, will continue to be about the same as in the sixties as a whole, averaging 262,000 a year. This rise will exceed that of any previous period other than the latter half of the sixties, when the average year-to-year increase reached a peak at 335,000.

Population in the college age group will grow only one-third as rapidly in the decade ahead as in the sixties. It is expected, however, that the portion entering college will continue to rise, as more 18-year olds graduate from high school, and a larger share of them go on to college. Reinforcing these influences, for public institutions, will be a continuation of enrollment gains above those in private institutions. The projections envisage rates of increase for the two-year colleges somewhat higher than for other institutions, although the differential is less than in recent years.

Question may be raised as to whether educational policy in the seventies will reduce academic and financial barriers to college entrance to a greater extent than in the past. To promote equality of opportunity, some institutions have adopted open-admissions policies, providing open access for all high-school graduates and otherwise qualified persons—at least to community colleges, and some also to four-year institutions.[22] The projected enrollments foresee a rise in the portion of high-school graduates going on to college from 60 percent at present to 68 percent by the end of the decade. More widespread use of the open-door policy than now exists would very likely be accompanied by a rise in this percentage. An example at hand, perhaps somewhat atypical, is that of the City University of New York. According to a study by University researchers, in the first year after an open-admissions policy was introduced, the number of the city's high-school graduates going on to some form of full-time higher education rose from 57 percent in the previous year to 76 percent.[23]

Further lowering of financial barriers to college attendance could also result in higher enrollments, somewhat above the levels projected here. In some opinions, opportunities for free education (*i.e.*, at public expense) should extend beyond elementary and high schools at least through the two-year college level, and some institutions already follow this practice. Still other efforts to lower financial barriers take the form of attempts to provide additional student aids in the form of government-subsidized loans or direct grants to students. For example, proposals in the 1972

22. One organization which has endorsed the open-admissions policy for community colleges is the Carnegie Commission on Higher Education. (See *The Open-Door Colleges—Policies for Community Colleges*, McGraw-Hill, New York, New York, June 1970). In making this endorsement, the Commission commented as follows: "The community colleges have a particular role to play in assuring equality of opportunity to all Americans. The Commission, while supporting open access, does not believe that all young people either want higher education or can benefit from it . . ."
23. Reported in *The New York Times*, May 11, 1971, p. 43.

Federal budget for student aid in the form of grants, work-study payments, and loans would raise the number of students aided under Federal programs from 1.7 million in 1969–70 to 3.9 million in 1972–73.[24]

The costs of rising enrollments may be offset in part by the more effective use of existing resources. A study of the Carnegie Commission on Higher Education, examining the recent financial stringencies in public and private colleges, cited the need for higher education to get back to its historic rate of increase in per student costs (i.e., rates experienced from 1930 to 1960).[25] Among the principal sources of savings recommended by the Commission were holding costs per student down by generally halting creation of new Ph.D. programs and concentrating doctoral training and Federally supported research in fewer institutions; moving toward year-round operation to gain maximum use of capital facilities; cautiously raising the student-faculty ratio; re-examining faculty teaching loads; and improving management.

The Carnegie Commission also sees "windfall" changes that should automatically serve to dampen growth in spending for higher education. Faculty salaries, for example, are seen as rising less rapidly than private wages and salaries in the seventies, instead of more rapidly as in the sixties. The continuing shift of enrollments to two-year colleges will slow the rise in per student costs. And, finally, research expenditures by the Federal government, according to the Commission, are likely to rise less rapidly in the seventies than in the sixties generally, when the increase averaged 10 percent annually.

Projections—Higher Education

The projections assume that on the average, per student outlays—in real terms—will rise by 2.5 percent annually, the same rate as during the sixties as a whole. With general price effects included, the annual rate becomes about 6 percent for the decade ahead, as compared to 5.3 percent in the sixties. From 1970 to 1980, average per student operating costs would, under these assumptions, rise from $2,444 to $4,388, or about four-fifths (Table 3.10). Allowing for the increase in enrollments previously discussed, current operating expenditures for public institutions of higher education would rise by 192 percent, as compared to 346 percent from 1960 to 1970.

The indicated slackening in enrollment growth would have a similarly dampening influence on capital outlays. Studies of the U.S. Office of Education indicate that over a five-year period, each additional full-time student requires capital outlays of $7,867 (constant 1969–70 dollars), very close to expenditures in the sixties. Measured from 1969–70, however, to 1979–80, there would be a decline of close to 20 percent in constant dollar terms. Allowing for construction cost increases, this translates to an increase of about one-fourth, with current dollar capital spending rising from $2.7 billion in 1970 to

24. For a description of these and other Federal aids, see *The Budget of the United States Government, Appendix*, Fiscal Year 1972, pp. 446–449. For other Federal aid proposals, see *Quality and Equality: Revised Recommendations—New Levels of Federal Responsibility for Higher Education*, Carnegie Commission on Higher Education, McGraw-Hill, New York, June 1970. The Commission recommends Federal aids to public and private institutions of $10.6 billion in 1976–77 and $12.6 billion in 1979–80, primarily for student aid programs, cost-of-education supplements, and research.

25. *The More Effective Use of Resources, op. cit.*, pp. 16–19. It is to be noted that the Commission's data are based on a different concept of expenditure than the Bureau of the Census definition utilized in this study.

$3.4 billion in 1980. This rate of increase is less than one-tenth as great as that which occurred from 1959 to 1969.

Total current and capital expenditures for public institutions of higher education are projected to rise from $12.9 billion in 1970 to $33.2 billion by 1980. Thus while expenditures during the sixties more than quadrupled, the outlook for the seventies is for further expansion to about two and one-half times 1970 levels. Expressed in other terms, the annual rate of increase in higher education outlays during the seventies is shown as 10 percent, in comparison with 16 percent in the past decade.

Summary of Projections

Table 3.11 summarizes the projections for all categories of education, along with historical comparisons.

Table 3.10

State–Local Expenditures for Higher Education, by Object

Actual and Projected, Selected Fiscal Years, 1955–1980

Fiscal year[a]	Total, higher education	Current operation		Capital outlay
		Total current	Average per student[b]	
	Amount (millions, except per student)			
Actual:				
1955	$ 1,570	$ 1,258	$ 963	$ 312
1960	3,202	2,443	1,564	759
1965[c]	5,863	4,418	1,764	1,445
1970	12,924	10,219	2,444	2,705
Projected:				
1975	21,773	18,544	3,346	3,229
1980	33,185	29,830	4,388	3,355
	Percent increase, selected intervals			
1955–60	104	94	62	143
1960–65[d]	92	93	20	90
1965–70	120	131	39	87
1970–75	68	81	37	19
1975–80	52	61	31	4
1960–70	324	346	67	256
1970–80	157	192	80	24

a. Represents ending date of fiscal year.
b. Per full-time equivalent degree credit enrollment.
c. Beginning in 1965, expenditures for "atomic research," amounting to $292 million in that year, are excluded from higher education. Projections follow the new definition.
d. Percentages for 1960–1965 only are calculated on the older definition, which includes atomic research in both years.

Source: Actual expenditure data from U.S. Department of Commerce, Bureau of the Census, and the U.S. Department of Health, Education, and Welfare, Office of Education. Projections and computations by Tax Foundation. Projections of capital outlays are based on office of Education data, adjusted to the Bureau of Census concept and for the assumed rise in prices for capital purchases.

Table 3.11

Summary of State–Local Expenditures for Public Education

Actual and Projected, Selected Fiscal Years, 1955–1980

Fiscal year	All institutions	Type of institution: Local schools	Higher education	Other
	Amount (millions)			
Actual:				
1955	$ 11,907	$10,129	$ 1,570	$ 210
1960	18,719	15,166	3,202	351
1965	28,563	21,966	5,863	735
1970	52,718	37,461	12,924	2,332
Projected:				
1975	80,746	55,466	21,773	3,507
1980	116,877	78,875	33,185	4,817
	Percent increase, selected intervals			
1955–60	57	50	103	67
1960–65	53	45	83	109
1965–70	85	71	120	217
1970–75	53	48	68	50
1975–80	45	42	52	37
1960–70	182	147	304	564
1970–80	122	111	157	107
	Percent of total educational expenditures			
1955	100.0	85.1	13.2	1.8
1960	100.0	81.0	17.1	1.9
1965	100.0	76.9	20.5	2.6
1970	100.0	71.1	24.5	4.4
1975	100.0	68.7	27.0	4.3
1980	100.0	67.5	28.4	4.1

Source: Actual data from U.S. Department of Commerce, Bureau of the Census; computations and projections by Tax Foundation.

IV.

Expenditures for Public Welfare

Various concepts of "public welfare" yield wide-ranging estimates of dollar costs. Perhaps the broadest definition, developed by the Social Security Administration, places welfare expenditures under all public programs at $143 billion in fiscal 1970, an amount equal to 15 percent of the gross national product and 47 percent of all government outlays.[1] In this context, social welfare covers those activities that directly concern the economic and social well-being of individuals and families. Included are social insurance, education, public aid, health and medical, veterans programs, public housing, and miscellaneous welfare services such as vocational rehabilitation and child welfare. State–local units financed over $66 billion, or 46 percent of welfare activities so defined.

The scope of public welfare with which this section deals is more limited. Public welfare, as used here and as defined by the Bureau of the Census, covers "support of and assistance to needy persons contingent upon their need." Most aid is of two types: direct cash payments to the needy, and vendor payments to private suppliers for medical care and other services provided under welfare programs. Other public welfare spending includes the provision of direct services to the poor, such as institutional care of the needy, and administration of welfare activities. Services provided directly through government hospitals and health agencies, however, are classified under health and hospitals. Similarly, the various welfare-type services administered in local public schools are included under education, instead of public welfare. Based on this definition, all government outlays for public welfare in fiscal 1970 amounted to $17.5 billion, of which the state–local amount (including funds from Federal grants) came to $14.7 billion (Table 4.1).

Federal direct outlays consist mainly of payments under antipoverty programs authorized in the middle sixties. Slightly over half of state–local welfare expenditures are financed through Federal grants, and the states pay for about three-fourths of the state–local share of costs. The states also have the major role in administration and direct disbursement of funds. During the sixties the long-term trend toward the shifting of responsibility for welfare from local governments to state and Federal levels continued, and has, in fact, been accelerated in recent years. Among states, arrangements vary as to relative state–local responsibilities in the welfare area; in recent years, however, the states generally have moved in the direction

1. Alfred M. Skolnik and Sophie R. Dales, "Social Welfare Expenditures, 1969–70," *Social Security Bulletin*, December 1970, pp. 3–17. An additional $66 billion in welfare spending was attributed to private sources.

of taking over from local governments a greater share of responsibility.

Most state–local expenditures for welfare are under the Federal-state–local system known as public assistance. The basic program, which has been in effect since the late 1930's has been revised frequently, both by Federal law prescribing the conditions and terms of Federal financial participation, and by state enabling legislation.[2]

Numerous types of services are available under public assistance. The most significant are those providing cash living allowances for the needy, and medical assistance payments under the Medicaid program authorized by Federal law in 1965. Federal contributions for both types of aid are limited to persons qualifying in one of four categories: the aged (OAA), families with dependent children (AFDC), the disabled (APTD), and the blind (AB).[3] To aid needy persons who do not fall into one of these Federally aided groupings, the states maintain programs known as general assistance (GA).

The 1965 to 1970 Upsurge

The sixties marked a sharp reversal in long-term trends in public welfare expenditures, and the effects have been especially pronounced in recent years. From 1948 to 1960 growth in welfare spending was the lowest among any of the nine major state–local functions. Welfare declined as a portion of total state–local budgets, as well as in rela-

2. The public assistance program was authorized by the Social Security Act of 1935, the same legislation which established the social security system.
3. All those qualifying for money payments in one of the Federally aided categories are automatically entitled to medical assistance. In addition, the Federal government will also participate in aid to certain persons in such categories who do not need assistance for regular living expenses but who require medical care beyond their means.

Table 4.1

Expenditures for Public Welfare by Level of Government and Source of Funds

Fiscal Years 1960, 1965, and 1970

Level of government	Amount (millions)			Percentage distribution		
	1960	1965	1970	1960	1965	1970
	Direct expenditure—all governments					
Total	$4,462	$6,420	$17,517	100	100	100
Federal	58	105	2,837	1	2	16
State	2,221	2,998	8,203	50	47	47
Local	2,183	3,317	6,477	49	52	37
	State–local expenditures by source of funds					
Total	$4,404	$6,315	$14,679	100	100	100
Federal	2,070	3,098	7,818	47	49	53
State	1,622	2,302	5,110	37	36	35
Local	712	915	1,751	16	15	12

Source: Derived from reports of the U.S. Department of Commerce, Bureau of the Census.

tion to personal income.[4] In this 12-year period as a whole, welfare spending grew at the rate of 6 percent annually, modestly when viewed against an overall rise in state-local spending of 9 percent per year. During the first half of the sixties, welfare costs began to rise at a slightly faster rate, 7.5 percent annually, but proportionately to other categories. From 1965 to 1970, however, public welfare outlays rose from $6.3 billion to $14.7 billion or 132 percent, and represented the fastest growing of the major state-local service categories. The average annual rate of this rise, over 18 percent, was half again higher than the 12 percent increase registered for all state-local services. Thus for the first time since the early fifties, welfare expenditures rose to more than one-tenth of state-local budgets.

What brought about this unusual growth pattern? There were a number of influences. Two aspects, however, overshadow others. The one most discussed was the sudden, and unexpected, swelling in caseloads in the AFDC program, beginning in 1967. The other, of even greater dollar significance, was the expansion of medical assistance under provisions of 1965 Federal law authorizing the Medicaid program. Since all those eligible for living allowances are automatically eligible for medical care, the effects of these two variables were reinforcing.

Cash Living Allowances. Increases in cash living allowances took place as a result of rising caseloads as well as higher average payments.

The total number of recipients increased from 7.1 million in December 1960 to 13.8 million in December 1970, almost doubling (Table 4.2). This overall rise took place in spite of declines in the number of recipients in the aged, blind, and general assistance groups. Although the disabled category rose by 564,000 or 170 percent, the major source of the increase was in the AFDC category. The number on AFDC rolls more than tripled, rising from 3.1 million in 1960 to 9.7 million in 1970. This growth in the past decade of 6.6 million was over three times the increase which had occurred in the preceding 20 years. Moreover, four-fifths of the expansion occurred in the last half of the sixties. In comparison with annual increases in recipient families averaging 5.5 percent in the period from 1961 to 1966, the rate of increase jumped to 15 percent in 1967, gradually accelerating to a peak of 36 percent in 1970 over 1969.

Along with rising caseloads, increases in average payments per recipient of about one-third led to a volume of money payments of $8.4 billion in calendar year 1970, over 2½ times the amount expended in 1960. Average annual increases for the several categories ranged from 2.8 percent for the aged, to 8.8 percent annually for the general assistance category, with the dependent children group in a middle range at 5.7 percent per year. These payment changes reflect not only legislative increases, but changes in the extent to which public aid supplemented other income available to recipients.

Medical Assistance. The burgeoning in AFDC caseloads may well have been the most dramatic factor in the welfare scene in recent years. Medical assistance, however, had an even greater effect on dollar costs, especially when compounded with the growth in numbers to be served. While the increase in cash living allowances accounted for 40 percent of the rise in welfare spending

4. The relationship of spending for specific functions to total spending and to population and income is shown in Chapter VII.

Table 4.2

Number of Recipients and Money Payments under Public Assistance Programs[a]

Actual and Projected, 1960–1980[a]

Category	Actual			Projected[c]	
	1960	1965	1970[b]	1975	1980
	Number receiving living allowances (thousands)				
Total	7,098	7,802	13,814	18,711	21,197
Aged	2,305	2,087	2,082	2,049	2,009
Blind	107	85	81	76	69
Disabled	369	557	935	1,374	1,878
Dependent children	3,073	4,396	9,660	14,222	16,186
General assistance	1,244	677	1,056	990	1,055
	Money payments (millions)				
Total	$3,263	$3,996	$8,415	$14,504	$21,317
Aged	1,626	1,594	1,861	2,115	2,345
Blind	86	77	98	116	129
Disabled	236	417	985	1,913	3,397
Dependent children	994	1,644	4,852	9,476	14,030
General assistance	320	261	619	884	1,416
	Medical vendor payments (millions)				
Total	$522	$1,480	$5,591	$11,119	$15,698

a. Number of recipients as of December. Payments on a calendar year basis.
b. Excludes payments for emergency assistance and to intermediate care facilities made to some 168,000 persons in 1970, involving outlays of $402 million.
c. No adjustment has been made for effects of Federal legislation in 1972, serving to reduce state-local spending for the aged, blind, and disabled, as well as for medical payments.

Source: Actual data from U.S. Department of Health, Education, and Welfare; projections by Tax Foundation.

during the sixties, the rise in medical assistance represented 45 percent of the total increase.

The 1965 Federal law establishing Medicaid made long-run Federal participation in medical welfare costs conditional on state actions to set up Medicaid programs.[5] In general, the states acted quickly to do so. In the first three years following Congressional authorization of these programs, medical payments increased by more than 40 percent annually as the states implemented programs. In 1969, partly in response to cutbacks in Federal matching provisions, the increase fell to 14 percent over the previous year; the following year, however, the rise was again accelerated—to 19 percent. Thus from 1965 to 1970 medical welfare costs almost quad-

5. For a discussion of this law, and state responses, see *Medicaid: State Programs after Two Years*, Tax Foundation, Inc., New York, 1968.

rupled, rising at the annual rate of about 30 percent. According to Federal budget projections, these payments will increase by around 20 percent annually in fiscal years 1971 and 1972.[6]

Before the introduction of Medicaid, direct payments for medical care under public assistance were limited, and the state programs varied widely in the scope of services and eligibility conditions. Comprehensive data are lacking as to the number of persons receiving such care before 1967. By 1967, 5.2 million different persons received services under Medicaid; the number increased to 15 million in 1970, and is estimated at 19 million in fiscal 1972.[7] The sharply rising caseloads under Medicaid resulted largely from expansion in the numbers getting cash living allowances, discussed above. Although medical care is available to certain categories not receiving maintenance payments, it is estimated that over three-fifths of those receiving Medicaid are eligible for cash payments; Medicaid payments on behalf of this group amount to 69 percent of the total.[8]

The cost impact of the growth in Medicaid recipients was accentuated by factors affecting costs per recipient. The scope of medical services available to clients was enlarged, as Federal law provided for coverage of services for which Federal matching aid was not formerly available. Further, Medicaid programs—like other health and medical programs—were affected by the rapid increases in medical and health care prices generally.[9] (See page 63.)

Other Welfare. While maintenance and medical payments make up the great bulk of public assistance outlays, spending for related purposes has also been climbing almost as fast, rising from $1 billion in 1960 to $2.3 billion in 1970. Included in this category are payments for institutional services in intermediate care facilities, social services, administration, employee traning, and other services. As noted below, some of these activities were affected directly by recent policy decisions.

Underlying Factors

Under a static program structure, some of the forces influencing trends in the number receiving public aid may be viewed as built-in, automatically responding to demographic and economic change. Differential population growth among age groupings was especially pronounced during the fifties, when the number of persons over 65 and under 18—the two age segments which constitute the vast majority of all public aid recipients—grew at twice the rate of growth in the total population and in fact accounted for three-fourths of the population increase. These disproportionate rates were sharply reduced in the sixties, but the effects were diluted by other concurrent developments. Despite an increase of more than 3 million in the over-65 age category, the number on OAA rolls dropped by 224,000 from 1960 to 1970, as rising numbers came under coverage of the Federal social security system. For other categories generally, however, and particularly the AFDC group, the numbers receiving aid grew more than proportionately to the eligible age groups (Appendix Table A.2). The population under 18 years old increased by 6.2 million from 1960 to 1970; at the same

6. *The Budget of the United States Government, 1972, Appendix*, p. 461.
7. *Ibid.*
8. *Ibid.*
9. About 67 percent of medical assistance payments are made to hospitals and nursing homes, 12 percent for physicians' fees, and about 8 percent for drugs. *Ibid.*

time the number of AFDC recipients (children and associated family members) grew by 6.6 million.

Although age specifications are a limiting factor under most categorical programs, age is by no means the only population characteristic related to the size of welfare rolls. Some theories link growing caseloads with migration patterns—e.g., from rural to urban centers; changing social mores leading to a breakdown in family life with a corresponding increase in the number of female-headed families; and other characteristics. While such influences probably contributed to welfare caseload increases, it has not been demonstrated that their depature from earlier patterns was so marked in recent years as to account for the sharp upsurge in AFDC rolls.

The effects of economic trends alone are similarly difficult to ferret out. Short-term cyclical swings, affecting income and unemployment, undoubtedly have some effect on welfare caseloads. General assistance rolls in particular tend to follow swings in the business cycle. But unemployment declined steadily in the years from 1965 to 1969, as AFDC caseloads were rising rapidly. Long-term changes in the level and distribution of income seem to have even less relationship to the number of public assistance recipients. Per capita real personal income rose by 35 percent in the decade of the sixties. Moreover, except for a slight setback in 1970, the number of persons below the poverty level consistently trended downward during the sixties, both in absolute numbers and in proportion to the population at large (Table 4.3).[10] In 1960 the number of welfare recipients was equal to 18 percent of the number classified as poor; by 1970 the number had risen to 54 percent.

Table 4.3

Persons below the Poverty Level[a]

Selected Years, 1959–1970

Year	Number (millions)	Percent of population
1959	34.5	22.4
1960	39.9	22.2
1965	33.2	17.3
1969	24.3	12.2
1970	25.5	12.6

a. See footnote 10 for this concept of "poverty."
Source: U.S. Department of Commerce, Bureau of the Census.

Clearly the search for a tenable explanation of welfare trends must extend beyond an examination of demographic and economic fluctuations. Among other factors, public policy decisions have been identified as influential. Such decisions fall into two groups: those primarily directed to other government programs, but having a spillover effect on public assistance; and those designed to change the public assistance program itself.

Spillover Effects of Other Programs. The Senate Appropriations Committee in 1970 heard testimony to the effect that some of the increase in welfare caseloads grew indirectly out of programs established under the Economic Opportunity Act of 1964, as well as from urban renewal projects. A representative

10. This measure of poverty, developed by the Social Security Administration, is defined by a variable income criterion, taking into account family size, composition, farm-nonfarm residence, and the proportions of income required to purchase a minimum adequate diet. A four-person nonfarm family was considered below the poverty threshold in 1969 if its annual income was less than $3,743. For a full discussion of the SSA poverty index, see Mollie Orshansky, "Counting the Poor: Another Look at the Poverty Profile," *Social Security Bulletin*, January 1965; and "Who's Who among the Poor: A Demographic View of Poverty," *Social Security Bulletin*, July 1965.

of the U.S. Department of Health, Education and Welfare testified as follows:

> Community action groups formed to help the poor, such as the National Welfare Rights Organization (NWRO), and the civil rights movement in general have contributed to a greater awareness by the poor of their legal entitlement to public assistance. As a result, applications for welfare have been rising, and a higher proportion of applications are usually being approved. Representatives from various community organizations have accompanied the applicant to the local welfare office to help in achieving approval of the application . . .
>
> Urban renewal has often resulted in an increase in the number of welfare recipients. Poor families, forced to move to different quarters, can no longer get by on their low income and have to seek assistance because of higher rent and the separation of sub-families that formerly lived in a single household and shared their total income.[11]

This testimony was primarily aimed at supporting far-reaching welfare reform. It is to be noted, however, that similar views have been widely expressed by others. For example, Piven and Cloward have noted that:

> . . . Not least, the welfare rise coincided with the enactment of Federal programs intended to restore calm to the ghettoes (especially the anti-poverty program) which, among the other things, hired thousands of poor people, social workers, and lawyers who helped families to obtain relief. The result was that the rolls quickly doubled . . .[12]

Public Assistance Program Changes. These influences emanate from three sources: (1) Federal legislation; (2) court decisions; and (3) state actions in implementing Federal law.

(1) Federal legislation. The 1967 amendments to the Social Security Act contained a number of provisions affecting both future caseloads and costs.[13] Among them are:

(a) Provision for disregarding work-connected expenses of recipients in computing payments, resulting in some families receiving aid longer than they would have otherwise;

(b) Work-incentive provisions for disregarding the first $30 per month per family of earned income plus one-third of the remainder of earnings in determining need;

(c) The requirement that all state programs include foster care under AFDC for specified groups of children (effective July 1, 1969);

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11. John M. Twiname, Administrator of the Social and Rehabilitation Service, U.S. Department of Health, Education, and Welfare. U.S. Senate, Hearings before the Committee on Appropriations, H.R. 18515, 91st Congress, 2nd Session, August 19, 1970, p. 3603.
12. Frances F. Piven and Richard A. Cloward, "Welfare I: A Political Response," *The New York Times*, November 15, 1971, p. 41. For other discussion of the activity of the National Welfare Rights Organization, see Gilbert Y. Steiner, *The State of Welfare*, The Brookings Institution, Washington, D.C., 1971, pp. 280–313.
13. Ironically, this legislation was aimed in part at reducing the number of welfare recipients in two ways: imposing a mandatory "freeze" on the number of children for whom the Federal government would make matching AFDC payments (subsequently repealed); and provision for a loss of benefits by welfare recipients unless they accepted offered jobs or took job training—the so-called work-incentive program. For a fuller discussion of these amendments, see *Public Welfare Programs: Issues, Problems, and Proposals*, Tax Foundation, New York, 1969, pp. 8–10.

(d) Provision for Federal financial participation in vendor payments to intermediate care facilities (institutions providing care less than that furnished in a skilled nursing home) under adult programs; and provisions of emergency assistance to families with dependent children, including migrant families, in danger of destitution.

(e) Requirement that states develop programs to improve social services to recipients and potential recipients.[14]

In addition to these provisions, the Medicaid program, enacted by Congress in 1965, had side effects on maintenance rolls. The inspection of nursing homes by review teams under the Medicaid program is said to have revealed that some patients lack income needed to purchase personal incidentals and are eligible for a money payment.[15]

(2) Court decisions. Based on Federal court decisions, HEW has issued regulations prohibiting states from requiring support from persons not legally liable for support under state law and from assuming as income in determining need the amounts that are not actually available. These policies have resulted in the addition of persons to the rolls and higher payments to persons previously on the rolls.

On April 21, 1969, another Supreme Court ruling removed durational residence requirements as an eligibility condition for maintenance assistance. The 38 states which previously had such residence requirements have thus been affected by the new policy.[16]

(3) State actions. No full rundown on recent state legislation on public assistance programs is available. As noted above, the states were required to implement some of the recent changes in Federal law as a condition of receiving financial aid. A great deal of activity in state legislatures in recent years was devoted to implementation of Medicaid, and 48 now operate Medicaid programs (Alaska and Arizona do not). By 1971, 31 states had set up programs for intermediate care facilities, and 20 for the new emergency assistance program as provided in the 1967 Federal law.

In response to Federal directives, some states also relaxed eligibility standards, shortened waiting periods for eligibility, and simplified enrollment procedures.

Recent Developments

State actions on welfare programs have recently taken a different direction, aimed at holding costs down, and limiting future growth. At least 20 states introduced cutbacks in welfare programs in 1971.[17] These efforts may account to some degree for the relative stability in caseloads in recent months.[18] It is too early to tell whether these latest developments will have lasting effects. They appear to demonstrate, however, that the states may have more

14. These services include those related to employment or training, child care, foster care, family counseling, homemaker services, money management, and others. They are available to welfare recipients and those who have been or might become welfare recipients. Sharp increases in expenditures for social services (for which the Federal government generally pays 75 percent of the total costs) led Congress to place a $2.5 billion ceiling on Federal funding for social services effective in fiscal 1973 (*H.E.W.* Fact Sheet on the Social Services Section of the State and Local Fiscal Assistance Act of 1972).
15. Twiname, *op. cit.*, p. 3603.
16. *Ibid.*, p. 3604.
17. *Washington Report*, American Public Welfare Association, Vol. 6, No. 4 (November 19, 1971), Washington, D.C., p. 1. The *Report* also noted that payments had been increased in 8 states.
18. In contrast to a rise of 17 percent in the 12 months ending in June 1971, the number of welfare recipients rose only 5 percent in the succeeding 12 months. *H.E.W. News*, U.S. Department of Health, Education, and Welfare, October 18, 1972.

latitude in influencing welfare costs than is generally ascribed to them.

On the whole, however, it is future Federal policy which is likely to have a more pronounced influence on welfare programs than state actions or basic economic and demographic changes. Numerous proposals in the past have called for the Federal government to assume a larger share of welfare costs than it now pays. For example, the Advisory Commission on Intergovernmental Relations has recommended Federal takeover of welfare and Medicaid costs with uniform standards, leaving the administration in the hands of states and localities; and the National Governors' Conference has urged full Federal financing of welfare.[19] The Committee for Economic Development has urged that the Federal government undertake a substantially higher proportion of the funding of public assistance with a view to a complete takeover of state and local public assistance costs over the next five years.[20]

Prospects for significant revision in the Federal role in welfare in the near future were dimmed by action in the 92nd Congress. While many changes were introduced, the Senate failed to approve the major "reform" proposal—an income-maintenance or "family assistance" plan—passed by the House. If approved, this provision would have resulted in sizable savings to states and localities, through greater Federal financial participation in the AFDC program. The compromise measure which finally emerged will have mixed effects, some tending to raise state–local welfare costs, and some to lower them.[21]

The major welfare provisions affect aids for the adult categories and Medicaid costs. The law replaced the present state programs of aid to the aged, blind, and disabled, effective January 1, 1974 with a new wholly Federal program of supplementary security income. Under the law, aged, blind, and disabled persons with no other income would be guaranteed a monthly income of at least $130 for an individual or $195 for a couple. In addition, the law provides that the first $20 per month of social security or other income would not cause any reduction in supplemental security income payments. States wishing to pay an aged, blind, or disabled person amounts in addition to the Federal supplemental security income payment would be free to do so. It is estimated that Federal costs of implementing cash benefit provisions for the adult categories will be $1.8 billion higher (in 1974) than under previous law.

Among provisions affecting Medicaid were several tending to moderate the expansion in state-local costs. These included: (1) coverage of the disabled under Medicare; (2) imposition of premium, copayment, and deductible requirements on Medicaid recipients; and (3) removal of the requirements (a) that states maintain their year-to-year fiscal efforts in Medicaid and (b) that states move toward a comprehensive Medicaid program by 1977.

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19. Advisory Commission on Intergovernmental Relations, Twelfth Annual Report, *Federalism in 1970*, Washington, D.C., 1971, p. 3.
20. *Improving the Public Welfare System*, A Statement by the Research and Policy Committee, Committee for Economic Development, New York, 1970, pp. 20–21.
21. H.R. 1, "Social Security Amendments of 1972," as approved by the Congress, October 17, 1972. See Appendix tables A.3 and A.4 for some major provisions and cost estimates.

Table 4.4

Summary of State-Local Expenditures for Public Welfare

Actual and Projected, Selected Fiscal Years, 1955–1980
(Dollar Figures in Millions)

Fiscal year	All public welfare	Cash assistance	Medical vendor payments	All other[a]
Actual:				
1955	$ 3,168	$ 2,598	$ 212	$ 358
1960	4,404	3,307	493	604
1965	6,315	3,922	1,367	1,024
1970	14,679	7,382	5,042	2,255
Projected:				
1975	27,128	13,419	10,027	3,682
1980	39,460	19,723	14,156	5,581
	Percent increase, selected periods			
1955–60	39	27	133	69
1960–65	43	19	177	70
1965–70	132	88	269	120
1970–75	85	82	99	63
1975–80	45	47	41	52
1960–70	233	123	923	273
1970–80	167	167	182	147

a. Includes payments for institutional services in intermediate care facilities, social services, administration, employee training, and other services.

Source: Actual data from U.S. Department of Commerce, Bureau of the Census. Computations and projections by Tax Foundation.

Projections

The projections developed here were made prior to Congressional approval of H.R. 1, and thus make no allowance for the effects of that legislation.[22] The estimates are based on the assumption that expansion in recipients and average payments per recipient will be generally commensurate with those of the sixties as a whole.[23]

The number of recipients of money payments is projected to rise from 13.8 million in 1970 to 18.7 million in 1975 and 21.2 million in 1980 (Table 4.2). For the decade, the rate would be only a little more than half the rate experienced during the sixties. The AFDC

22. Gross Federal costs of assuming the responsibility for financing cash allowances under the adult categories are estimated at $3.5 billion in 1964 (see Appendix table A.4). The states and localities may supplement the basic Federal allowance; but, on balance, state–local expenditures for those categories will be significantly lower than in the absence of the new legislation and the projections thus tend to over-state spending for these purposes. The difference, however, as regards the projections, appears to have been absorbed by the end of fiscal year 1972. In fiscal years 1971 and 1972, respectively, total welfare spending increased by 27 percent and 17 percent respectively. *H.E.W. News*, U.S. Department of Health, Education and Welfare, October 18, 1972.

23. A notable exception is that it is assumed that the rise in AFDC caseloads will be slower in relation to the eligible population age group. See Appendix A.2. This assumption appears to be borne out by recent trends. In the 12 months ending in June 1972, AFDC recipients increased by 7 percent, as compared with a 21 percent rise in the previous year. *Ibid.*

category is seen as continuing to account for ever larger segments of the total, with the OAA group continuing to decline both in absolute numbers and in relation to the population aged 65 and over.

With average payments per recipient growing as in the past decade, total cash living allowances would rise from $7.4 billion in 1970 to $19.7 billion in 1980, at a faster pace than in the sixties as a whole, but not nearly so rapidly as in the years since 1965.[24]

Projections of medical payments and other services, on the other hand, are seen as rising at rates significantly lower than in the past decade, proportionally to increases in both caseloads and medical care prices. As noted above, recent growth in these programs reflects the effects of implementing new legislation introduced in the latter half of the sixties (e.g., Medicaid, intermediate care facilities, emergency aid, strengthened social services). It seems unlikely that these programs will continue to expand at such sharp rates as during the implementation period.

The over-all projections, on a fiscal-year basis, appear in Table 4.4. Total state–local public welfare outlays, according to the projections, would rise from $15 billion in 1970 to $27 billion in 1975 and $39 billion in 1980, an annual rate of 10.4 percent, as compared to a rate of 12.8 percent in the sixties as a whole, but far less than the 18 percent increase registered in the period from 1965 to 1970. The annual rate of rise is indicated at 13.1 percent for the first part of the seventies, gradually slowing to 7.8 percent for the remainder of the projection period.

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24. These data, as shown in Table 4.4, are on a fiscal year basis and therefore differ from calendar year data depicted in Table 4.2.

V.

Expenditures for Health and Hospitals

The states and localities play an important role in both financing and administering health and hospital programs. The conceptual organization of this study places emphasis on the administrative role; that is, on the dollar amounts spent for services provided by state–local agencies, without regard to the source of funds. The projections also conform to this definition. An examination of the financial aspect, however, may serve to put the administrative role into clearer focus.

Financial Role

More than $8 billion in state–local tax funds go to the support of health and medical services under a variety of programs (Table 5.1). The largest amounts are for general hospital and medical care and medical services under public assistance programs. Medical and health services are also provided under programs of workmen's compensation, maternal and child health, school health, and others. Medical research and construction account for the remainder of state–local outlays for health and medical care.

Medicare and Medicaid introduced vast changes in financial arrangements for health and hospital care, and were partially responsible for a near-tripling

Table 5.1

Expenditures for Health and Medical Care from State–Local Funds, by Program[a]

Fiscal years 1965 and 1970

Program	Amount (millions)		Percent of total	
	1965	1970[b]	1965	1970
All programs	$4,910	$8,315	100.0	100.0
Health and medical services, total	4,566	7,772	93.0	93.5
Public assistance (medical)	812	2,527	16.5	30.4
General hospital and medical care	2,378	2,916	48.4	35.1
Maternal and child health	154	215	3.1	2.6
School health	142	263	2.9	3.2
Other public health	448	802	9.1	9.6
Miscellaneous[c]	632	1,049	12.9	12.6
Medical research	55	73	1.1	.8
Medical facilities construction	289	470	5.9	5.7

a. Excludes amount spent at state–local institutions but financed from private or Federal funds.
b. Data for 1970 are preliminary. The revised total for the year is $8,434 million, but details by program are not yet available.
c. Includes medical benefits under programs of temporary disability insurance, workmen's compensation, and medical vocational rehabilitation.

Source: U.S. Department of Health, Education, and Welfare, Social Security Administration.

Table 5.2

Financing of All Health Expenditures, by Source of Funds[a]

Selected Fiscal Years, 1960–1970

Source of funds	1960	1965	1970
Total health expenditures (billions)	$ 26.4	$ 38.9	$ 67.8
Percent of personal income	6.7	7.6	8.7
Percentage distribution of source of funds	100.0	100.0	100.0
Private	75.7	75.5	63.1
Federal	11.1	11.9	24.5
State and local	13.2	12.6	12.4

a. This concept of expenditure is not directly comparable to Bureau of the Census data presented elsewhere, mainly because the series here includes some health and medical services which the Census Bureau does not classify as "health and hospitals." See text definition.

Source: U.S. Department of Health, Education, and Welfare, and U.S. Department of Commerce. Computations by Tax Foundation.

of total health expenditures during the sixties. Outlays for all health services rose from $23.4 billion in 1960 to $67.8 billion in 1970, by two percentage points as a share of personal income (Table 5.2). It is somewhat surprising that these developments had little effect on the share of the nation's health bill paid by state–local units. In 1960 these institutions provided about 13 percent of all health funds; by 1970 the amount had declined by only 1 percentage point. In this respect, the predominant effect of Medicare and Medicaid was to double the share of Federal spending in health care, with a corresponding reduction in the portion financed privately—by consumers directly or through private insurance or philanthropy. Whereas Federal funds paid for around 12 percent of all health outlays in 1965, the share rose to 25 percent in 1970, as the private share fell from 76 percent to 63 percent.

The new financial arrangements, however, did affect the allocation pattern of state–local funds among health programs. In particular, the share of the health dollar directed toward general hospital and medical care declined substantially, as medical spending for welfare programs (including physicians' services, nursing home care, etc.) increased sharply.

Administrative Role

State and local governments own and operate 2,257 hospitals, almost one-third of the nation's total. Around 1,700 for these are under local government control (counties, cities, special districts), and the remainder are state institutions. On an average daily basis, there were over 630,000 patients in state–local hospitals during 1970, more than half the number in all non-Federal hospitals. (See Table 5.3.) While there are more short-term general hospitals (1,704) than any other type, the large majority of patients are those requiring long-term care. Over two-thirds of the total are in psychiatric hospitals.

Concepts and Definitions. The Bureau of Census concept of health and hos-

pitals, used in the projections in this study, differs in two major respects from the classification discussed previously in relation to all national health expenditures. (1) The Census data for health and hospitals comprise direct outlays of state and local governments without regard to the source of funds—e.g., from patients' charges and fees, Federal grants, and state–local tax revenues—whereas the national health data reflect only those amounts paid from state and local tax revenues. (2) The Census data for the category health and hospitals are exclusive of health and medical outlays administered by agencies of government other than departments of health and hospitals.[1] In view of these differences, it is somewhat surprising that the two sets of data are not more divergent than they are. Under all functional classifications, state and local jurisdictions paid $8.4 billion of the national health bill in fiscal year 1970, as indicated in Table 5.1. On the Census basis, state agencies in the fields of health and hospitals administered direct outlays of $9.7 billion (Table 5.7).

Under the Bureau of Census concept, expenditures for "hospitals" include the following: the establishment and operation of hospital facilities, provision of hospital care, support of other public or private hospitals, and outlays of hospitals (though not infirmaries) operated

1. Major categories excluded are medical vendor payments under public welfare programs; health services provided by dentists, doctors, nurses, etc. employed in local schools and in university infirmaries; and medical benefits under social insurance programs, notably temporary disability insurance and workmen's compensation programs.

Table 5.3

Trends in State–Local Hospital Patients and Expenses

Calendar Years 1965 and 1970

Category	Number or amount		Percent of nation's total	
	1965	1970	1965	1970
	Patients in state–local hospitals			
All hospitals	783,712	630,350	62.6	53.9
Psychiatric	590,988	432,520	97.3	96.8
Tuberculosis	24,379	11,820	93.6	97.0
Long-term general	37,770	36,966	67.2	75.2
Short-term general	130,575	149,044	23.2	22.5
	Hospital expense (millions)			
All hospitals	$3,923	$7,356	34.5	31.9
Psychiatric	1,522	2,465	91.6	90.9
Tuberculosis	155	146	93.9	96.1
Long-term general	252	417	62.1	65.1
Short-term general	1,994	4,328	21.8	22.1

Source: American Hospital Association.

Table 5.4

Selected Factors Affecting Hospital Costs[a]

Selected Calendar Years, 1960–1970

Factor	1960	1965	1970
Admissions (thousands)	22,970	26,463	29,252
Per 1,000 population[b]	128	137	144
Occupancy (percent)	74.7	76.0	78.0
Average length of stay (days)	7.6	7.8	8.2
Personnel[c]			
Total number (thousands)	1,080	1,386	1,929
Per 100 patients	226	246	292
Hospital expense:			
Total (millions)	$5,617	$9,147	$19,560
Per patient day[d]	32	44	81
Per patient stay[e]	245	346	669

a. Non-Federal short-term general and other special hospitals.
b. Total population as of July 1.
c. Full-time personnel plus full-time equivalents of part-time personnel.
d. Total expense divided by the number of in-patient days.
e. Total expense divided by the number of admissions.
Source: American Hospital Association.

in conjunction with institutions of higher education. For "health," expenditures cover health research clinics, nursing, immunization, maternal and child health, crippled children's programs, and general public health activities such as the inspection of water supply, food handling establishments, and water pollution control. Only those school health services provided by health agencies are included.

Recent Trends

Notwithstanding conceptual differences, the Census Bureau's series on state–local health and hospital expenditures, as defined above, generally followed the trends depicted in the data on all national health outlays during the sixties. These trends were remarkably similar, as a matter of fact, to over-all growth in the state–local government sector. Expenditures rose from $3.8 billion in 1960 to $9.7 billion in 1970, an average annual rate of 9.8 percent.[2] As in other categories, there was a marked acceleration in the growth rate beginning about 1965. In the first half of the sixties, increases were moderate, at just over 7 percent a year. In the ensuing five years the average rate per year rose to 12.5 percent. These increases exceeded the concurrent rise in personal income and general population.[3] The share of hospital and health services in over-all state–local budgets, however, remained stable.

Although hospitals account for more than four-fifths of the health-hospitals combined expenditure total, it is in the health classification that increases have been largest in recent years.

2. Historical data on expenditures appear in Table 5.7, along with the projections.
3. See Chapter VII for comparative data.

Underlying Factors

Selected factors affecting short-term hospital costs during the sixties appear in Table 5.4. Per capita admissions to hospitals continued to rise in relation to the total population. Occupancy rates rose slightly. The average length of stay for patients, which had previously declined in the postwar period, resumed its rise. Moreover, the number of hospital employees attending patients continued its long-term upward trend. In 1970 there were 292 employees per 100 patients (average daily census), as compared to 226 in 1960. These and other influences led to a rise in hospital expense per patient day from $32 in 1960 to $81 in 1970, with the largest part of the rise occurring in the past five years. The average patient's hospital bill in 1970 was $669, nearly three times as much as ten years earlier.

Effects of Medicaid and Medicare. The introduction of Medicare and Medicaid in the mid-sixties triggered widespread predictions of decline in the role of state–local hospitals. The aged and the indigent, it was said—given the right to seek care from providers of their own choosing—would tend increasingly to choose private facilities, thus leading to a decline in utilization of state–local hospitals. Have these predictions materialized? Available evidence suggests that although there has been some decline, it has not been as great as expected, and may already have spent its force. Two sets of data bear out this conclusion:

1. In an analysis of trends in 14 large urban public hospitals, Dr. Paul Ellwood, Jr. found that annual admissions declined by 9.5 percent from 1965 through 1968.[4] He noted, however, that three-fourths of the loss occurred in the first full year of Medicare and Medicaid, and that in the following year, 1968, admissions fell less than one percent—and actually increased in half of these hospitals. In Dr. Ellwood's view, public hospital utilization is likely to accelerate again as hospitals become more patient oriented, and city and county hospitals find ways to make their facilities more attractive to middle-class patients.

2. As shown in Table 5.3, the role of state–local institutions in hospital care declined somewhat from 1965 through 1970, based on both patient loads and outlays. This trend, however, reflects almost solely the sharp decline in psychiatric and tuberculosis cases in the average daily census of all hospital cases. For the short-term general hospital sector, in which increasing competition from the private sector might have been expected with the advent of Medicare and Medicaid, outlays at state–locally owned facilities as well as patient loads, remained virtually unchanged at around one-fifth of the total.

As a result of these developments, the administration of short-term general hospitals has claimed a growing share of attention in the hospital programs of states and localities. Emphasis on specialized treatment of psychiatric, and to a lesser extent, tuberculosis cases has been reduced as public general-care hospitals have become more important. In 1960, 43 percent of receipts at state–local hospitals were for services rendered at short-term general hospitals; by 1965 the portion moved up to 50 percent and by 1970 to 59 percent.

Medicare and Medicaid thus do not appear to have had a significant effect on lowering the demand for services in state–local general hospitals. The

4. Paul M. Ellwood, Jr., M.D. and Earl J. Hoagberg, *Hospitals, Journal of the American Hospital Association*, July 1, 1970, Vol. 44, p. 49.

Table 5.5

Medical Care Prices

Selected Years, 1955–1970
Index Numbers, 1957–59 = 100

Year	All medical care[a]	Physicians' fees	Hospital daily service charge	Prescriptions and drugs
1955	73.4	76.0	57.8	86.6
1955	88.6	90.0	83.0	92.7
1960	108.1	106.0	112.7	102.3
1965	122.3	121.5	153.3	98.1
1966	127.7	128.5	168.0	98.4
1967	136.7	137.6	200.1	97.9
1968	145.0	145.3	226.6	98.1
1969	155.0	160.0	267.9	99.6
1970	164.9	167.0	287.9	101.3

a. Includes items not shown separately.
Source: U.S. Department of Labor, Bureau of Labor Statistics.

major long-run effect may be of an entirely different nature, setting a challenge to state–local institutions to meet the same standards as those provided by voluntary hospitals. As one observer noted, "second-class service" is rapidly becoming unacceptable to even the indigent patients now almost exclusively identified with public hospitals, for the poor are now demanding the same quality and quantity of health services as those available to the more affluent segments of society.[5]

While state–local support of health and hospitals under all programs kept pace with national trends, as did outlays at state–local hospitals, the rise in hospital expenditures *financed* by the state–local taxpayers was far less.[6] Total private and government expenditures for hospital care rose from $13.5 billion in 1965 to $23.9 billion in fiscal 1969, or over three-fourths.[7] At the same time the increase in state–local support of general hospital and medical care (excluding such care under special programs, such as public assistance) rose by just over one-fifth. This financial development has led to complaints of inadequate financing by some administrators, who hold that the tax support of the public hospital's budget has increased very little in recent years, despite rapid increases in costs, and that the cities and counties have treated the payments from Medicare and Medicaid "as a windfall for the taxpayer rather than a means of shoring up the finances of the public hospital."[8]

5. *Editorial Notes*, *Journal of the American Hospital Association*, July 1, 1970, vol. 44, p. 39.
6. Based on the Bureau of Census concept, charges and fees imposed by state–local hospitals brought in amounts equal to 27 percent of hospital outlays in 1960 and 39 percent in 1970.
7. "National Health Expenditures, Fiscal Years 1929–70 and Calendar Years 1929–69," Research and Statistics Note No. 25—1970, December 14, 1970, U.S. Department of Health, Education, and Welfare, Social Security Administration.
8. Ray E. Brown, "The Public Hospital," *Hospitals, Journal of the American Hospital Association*, July 1, 1970, p. 41. This view was echoed by a number of hospital administrators in a series of articles on "The Plight of the Public Hospital" in the same publication.

Medical Care Prices. The rise in medical care prices in recent years has been so widely documented as to require little elaboration here. In the last half of the sixties annual increases in the over-all medical care component of the consumers price index exceeded 6 percent. The rate of expansion in hospital daily service charges—of particular importance in state–local services—was especially pronounced, and averaged over 13 percent between 1965 and 1970 (Table 5.5).

These price increases, measured against growth in hospital outlays, raise question as to what, if any, increase occurred in the real quantity and quality of hospital services. Table 5.6, based on data and methodology developed by the Social Security Administration,[9] attempts to provide some perspectives, for the period from 1965 to 1969. For short-term general hospitals, rising prices accounted for over three-fourths of the $1.6 billion expenditure rise in this period; growth in total population had relatively slight influence; and all other factors—the rise in the real quantity of services, as through increasing per capita utilization, and in quality—accounted for about one-sixth of the rise in expenditure. These results suggest that, in the period represented, the rise in quality and scope of services per member of the population averaged 2.7 percent per year.

For all mental hospitals (97 percent of whose patients are in state–local facilities), the raw figures suggest perhaps larger rates of increase in productivity, as illustrated by several developments. These include: increase in

9. See *Sources of Increase in Selected Medical Care Expenditures, 1929–1969*, Staff Paper No. 4, U.S. Department of Health, Education, and Welfare, Social Security Administration.

Table 5.6

Analysis of Sources of Increase in State–Local Short-Term General Hospital Expenditures

Fiscal Years 1965–1969

Source of income	Average annual increase 1965–69 (percent)	Distribution by source of increase	
		Amount (millions)	Percent of total
Total expenditures	16.1	$1,630	100.0
Prices[a]	12.3	1,245	76.4
Population	1.1	110	6.8
All other[b]	2.7	275	16.8

a. Based on expenditures per patient day, adjusted for changing mix of outpatients to patients in hospital.

b. Residual representing change in per capita utilization and quality of services.

Source: Basic hospital and price data from Social Security Administration; computations by Tax Foundation.

Table 5.7

State–Local Expenditures for Health and Hospitals

Actual and Projected, Selected Fiscal Years, 1955–1980

Fiscal year	Total, health and hospitals	Health	Hospitals
	Amount (millions)		
Actual:			
1955	$2,524	$ 471	$2,053
1960	3,794	559	3,235
1965	5,361	836	4,525
1970	9,669	1,806	7,863
Projected:			
1975	17,631	3,776	13,855
1980	29,914	7,594	22,320
	Percent increase, selected intervals		
1955–1960	50	19	58
1960–1965	41	50	40
1965–1970	80	116	74
1970–1975	82	109	76
1975–1980	70	101	61
1960–1970	155	223	143
1970–1980	209	320	184

Source: Basic data from U.S. Department of Commerce, Bureau of the Census. Computations and projections by Tax Foundation.

the total number of *admissions* as well as in the rate per thousand members of the population at large, from 2.3 in 1960, to 2.9 in 1965 and 3.3 in 1970;[10] and a decline in the average daily census of patients of 27 percent in the period from 1965 to 1970 (Table 5.3).

Projections

Along with other providers of medical and hospital services, state–local units have been victims of rapidly rising medical prices. The outlook for future expenditures depends heavily on the course of prices as well as on the ability to improve productivity of available medical and health resources. The projections assume that hospital and health costs will continue to rise somewhat more rapidly than consumer prices generally, but at rates below those experienced in the 1965–1970 period.

Table 5.7 presents the projections.[11] Total health and hospital expenditures of states and localities are projected as rising from $9.7 billion in 1970 to $29.9 billion by 1980, more than tripling, with the "health" category showing the greatest proportionate advance.

10. Data are from U.S. Department of Health, Education, and Welfare, as reported in *Statistical Abstract of the United States*, 1972, p. 74. The total days spent in mental hospitals based on the rate per thousand members of the population, declined from 1,261 in 1965 to 862 in 1970, about one-third.

11. See Appendix I for basis of derivation. The health and hospital projections, unlike those for other functions, are based on a continuation of real per capita increases corresponding to those of the period 1965–1970, instead of those for the sixties as a whole.

VI.
Expenditures for Highways and Streets

State–local units have responsibility for providing and maintaining some 3.8 million miles of highways and streets.[1] About one-fourth of the existing mileage has been constructed with partial support from the Federal government, and falls within what is known as the Federal-aid system. States and localities, however, finance upkeep and maintenance for the Federal-aid system and all costs of the 2.8 million miles outside the system (Table 6.1).

Among levels of government, the states have principal responsibility for both financing and administering highways. About one-half of highway funds derives from state sources, mainly motor fuel and vehicle taxes on highway users, supplemented by tolls on roads and bridges, general fund appropriations, and bond issue proceeds. Federal support, about 30 percent of the total, comes from Federal excise taxes on motor fuels and certain vehicles, dedi-

1. The Bureau of Census classification of highways, used in this study, includes provision and maintenance of highway facilities, including toll turnpikes, bridges, and tunnels and ferries, as well as regular roads, highways, city streets, street lighting, and snow and ice removal. Excluded from expenditures for highways under the Census concept are interest on highway debt, debt retirement, highway police patrols, and traffic safety.

Table 6.1

State–Local Road and Street Mileage in the United States Classified by Road Systems, December 31, 1971

(Mileage in thousands)

System	Total Federally aided and other	Not Federally aided	
		Mileage	Percent of total
Total	3,759	2,836	75
State highways, total	760	180	24
Primary system	469	28	6
Secondary system	134	49	37
County roads under state control	156	104	67
County roads	1,727	1,438	83
Town, township, and other local	530	523	99
City streets[a]	516	472	91
All other[b]	227	224	99

a. Municipal extensions of county, town, and township roads included.
b. State and national parks and reservation roads and toll facilities.
Source: U.S. Department of Transportation, Federal Highway Administration.

cated to the highway trust fund, established by law in 1956. The remaining 20 percent is collected by counties, townships, and municipalities largely in the form of property taxes, assessments, and other general revenue sources.

From an administrative standpoint, the states also have the dominant role, disbursing nearly three-fourths of highway funds, either directly or through local governments. Direct Federal expenditures for highways (less than 2 percent of all highway spending) are made only on roads in national parks, forests, and other roads owned by the Federal government, comprising about 5 percent of total highway mileage.

For many years capital costs have been by far the most expensive item in highway budgets. Capital investment—to enlarge, reconstruct, and modernize existing facilities—currently runs about twice the size of outlays for maintenance, administration, and other current operations.

Recent Trends

Although highways in 1970 remained the second most costly function of state–local units, their relative importance in the total declined during the sixties.[2] Highway outlays rose from $9.4 billion in 1960 to $16.4 billion in 1970, or 74 percent, less than half the rate experienced for all general functions. As a result, highway spending dropped successively from 18 percent of general expenditures at the beginning of the decade to only 12.5 percent in 1970. This recent budget share is approximately the same as existed in 1950 before the acceleration of the Federal-aid highway program (1956). Highway outlays have also declined in relation to personal income, although per capita amounts have steadily increased.

Other perspectives on highway finance during the sixties are depicted in Table 6.2. The rise in highway outlays was accompanied by increases in consumer expenditures for user-operated transportation, miles of vehicular travel, and motor vehicle registrations. There was very little increase in total highway mileage, as efforts were mainly on reconstructing and improving existing roads, especially those in the Federal-aid system. Inflationary trends were quite pronounced, particularly in the period from 1965 to 1970, when highway construction costs rose at the rate of almost 7 percent annually.

Thus it cost $1.39 in 1970 to buy the same physical volume of highway construction that $1 would buy in 1965. As a result, the real volume of capital input during the last part of the sixties declined (in spite of a $2.5 billion current-dollar increase). The real rate of increase in maintenance and other current operations was little more than 2 percent per year, as compared to the close to 8 percent per year current-dollar rise.

Receipts of highway-user taxes, both Federal and state-local, generally paralleled the rise in expenditures; Federal grants, however, slowed perceptibly in the latter half of the sixties. The volume of highway debt outstanding rose only about half as much as indebtedness for other government functions.

Federal Aid System

Although, as noted above, most highways and streets lie outside the Federal aid system, Federal highway policy since 1956 has played a major role in influencing state–local highway

2. In fiscal 1971, highways dropped into third place, behind education and welfare. Historical data on expenditures appear in Table 6.5, along with projections. Trends in outlays for all functions as a share of total budgets and in relation to population and income are shown in Chapter VII.

finance.[3] There are several different Federal highway grant programs, and the number has grown in recent years. Among the various programs, the major ones are the 42,500-mile system of Interstate and Defense Highways; and the primary, secondary, and urban (so-called ABC) system, which is not limited in mileage. Federal grants cover 90 percent of capital costs on the inter-

3. The most immediate effect, of course, is on capital outlays; however, once roads are improved to higher standards, maintenance costs, borne solely by state–local units, become higher.

Table 6.2

Selected Factors Affecting Highway Finance

Selected Years, 1960–1970

Factor	1960	1965	1970	Annual rate of change (percent) 1960–65	1965–70
Total highway mileage	3,546	3,690	3,730	.8	.2
Rural	3,116	3,183	3,169	.4	−.1
Municipal	430	507	561	3.3	2.1
Motor vehicle miles of travel (billions)	718.8	887.8	1,120.7	4.3	4.8
Motor vehicle registrations (thousands)	73,869	90,358	108,436	4.1	3.7
Consumer expenditures for user-operated transportation (millions)	$39,825	$54,356	$72,262	6.4	5.9
Highway maintenance and operation cost index (1967 = 100)	78.4	89.7	116.8	2.7	5.4
Highway construction cost index (1967 = 100)	80.1	90.3	125.6	2.4	6.8
Federal grants to state–local governments for highways (millions)	$ 2,935	$ 4,011	$ 4,520	6.5	2.4
State–local expenditures for highways, total (millions)	$ 9,428	$12,221	$ 16,427	5.3	6.1
Capital outlay	6,340	8,324	10,762	5.6	5.3
Maintenance	3,088	3,897	5,665	4.8	7.8
State–local highway debt (millions):					
Debt issued	$ 1,206	$ 1,070	$ 1,890	−2.4	12.0
Debt redeemed	616	855	1,271	6.8	8.3
Debt outstanding	13,166	15,316	19,008	3.1	4.4
Highway taxes (millions):[a]					
Federal	$ 1,984	$ 2,792	$ 3,776	7.1	6.2
State–local	5,068	6,476	9,228	5.0	7.3

a. Motor fuels, motor vehicle licenses, and operators' licenses.

Source: U.S. Department of Transportation, Federal Highway Administration; and U.S. Department of Commerce, Bureau of Economic Analysis. Computations by Tax Foundation.

Table 6.3

Status of Mileage in the Interstate and Defense Highway System[a]

As of September 30, 1972

Status	Number of miles	Percent of total	
		1972	1966[b]
Total designated for the system	42,500	100	100
Open to traffic, total	33,796	80	52
Completed to acceptable standards	28,957	68	39
Improved to presently adequate standards[c]	2,534	6	8
Toll facilities	2,305	5	6
Work in progress, total	7,374	17	42
Under construction	3,742	9	14
Engineering or right-of-way	3,632	9	27
Preliminary status or not in progress	1,330	3	6

a. Some $45 billion has been spent for the Federal-aid Interstate program since the accelerated program began in 1956.
b. As of March 31; the designated system totaled 41,000 miles in 1966.
c. Additional improvements are needed to meet full standards.
Source: U.S. Department of Transportation, Federal Highway Administration.

state system (somewhat more in those states with large areas of public domain) and match state funds on a 50-50 basis for the primary, secondary, and urban programs.

The Interstate System. Recent progress toward completion of the interstate system is shown in Table 6.3. In the past six years over 12,000 additional miles of the system have been opened to traffic, bringing the total open to nearly 34,000 miles, about four-fifths of the scheduled mileage. In 1966, only about half the system was open to traffic. Nationally, there remains a considerable amount of work in each of the process stages (construction, engineering, and right-of-way acquisition). Some states are quite close to completing their designated portion of the system; others have further to go.[4]

Several legislative and administrative developments in recent years affect the future of the interstate system. In 1968, Congress approved an increase in the designated mileage of the system from 41,000 to 42,500 miles. By 1970 it had become clear that the system could not be completed by the 1972 target date, and Congress extended the completion date through fiscal year 1976, at the same time extending the Highway Trust Fund for five years (to October 1, 1977), with Federal taxes continued at existing rates. Moreover, administrative estimates of the total costs of the system were also increased. Originally estimated to cost $27 billion, the inter-

4. For example, at the end of June, 1969, seven states had obligated funds for all preliminary engineering, and 30 states had 5 percent or less to be obligated. Five states had obligated all right-of-way and 13 had 5 percent or less to be obligated. *1970 National Highway Needs Report*, U.S. Department of Transportation, Federal Highway Administration, Bureau of Public Roads, Washington, D.C., December 1969, p. 26.

state system, according to 1972 projections, will cost $68.3 billion, 47 percent more than the amount estimated in 1965. The cost over-run, which will eventually prove even larger no doubt, is attributed to higher design standards, inflation, and added system miles.[5]

Other Federal Aid Systems. During the past six years an additional 61,000 miles in the Federal-aid ABC program were completed, bringing the total since July 1, 1956 to 272,000 miles completed, with construction or improvement of some 14,000 additional miles underway or authorized (Table 6.4). Cumulative investment for construction of these systems is close to $34 billion. Costs are presently shared on an approximately equal basis by Federal and state-local governments. (The 1970 Federal-Aid Highway Act changed the Federal share of ABC funds from 50 to 70 percent, effective July 1, 1974.)[6]

Table 6.4

Active and Completed Projects in the Federal-Aid Program of Primary, Secondary, and Urban Highways

As of September 30, 1972

Status	Number of miles	Total cost (billions)
Total	272,359	$33.7[a]
Completed since July 1, 1956	258,645	25.5
Underway or authorized	13,714	5.1

a. Includes $3.1 billion of work in the engineering or right-of-way acquisition stage, not shown separately.

Source: U.S. Department of Transportation, Federal Highway Administration.

Other Recent Developments

From 1965 through 1969 Federal highway disbursements to states and localities—for work completed on all systems—remained steady at close to $4 billion a year, about four-fifths of which was allocated to the Interstate System.[7] The scheduled amounts for distribution in the early part of the seventies are more than one-third larger, in view of Congressional action in recent years. In addition to increasing the annual amounts available for the interstate system and the regular ABC system, legislation introduced several new programs and expanded others. Included were programs for Appalachian roadbuilding; landscaping, scenic enhancement, and other beautification; new highway and motor vehicle safety; new urban traffic operations improvements (TOPICS) to reduce traffic congestion in urban areas; expanded aid to highways in rural areas; new Economic Growth Center highways; special highway employee training; bridge replacement; and a new urban system to help solve urban transportation problems.

A discussion of the full scope of these recent program developments lies outside the range of this study. Initial authorizations for Federal expenditure are relatively small, in comparison with most older programs, and some of the newer efforts are of an experimental or temporary nature. Two,

5. *1970 Needs Report, op. cit.*, p. 26.
6. For a fuller discussion of these and other highway financing arrangements, see *Highway Statistics, 1970*, U.S. Department of Commerce, Federal Highway Administration, pp. 64–68.
7. Although cutbacks, to restrain inflationary pressures and conform to Congressional mandates for Federal expenditures control, were ordered at intervals during each of the fiscal years 1967 through 1970, the amounts finally made available each year were equal to or greater than the projected amounts before the cutback. *1970 Needs Report, op. cit.*, pp. 51–52.

however, merit special comment: the new urban system and the bridge replacement program. The Federal-aid program in urban areas has heretofore been confined by law to extensions of the rural interstate and primary routes into and through the cities. The new system will consist of additional routes, to be selected cooperatively by local officials and state highway administrators. Congress authorized $100 million for the urban system for each of the fiscal years 1972 and 1973. These amounts are said to represent only a small fraction of sums needed, which are estimated at $4 billion annually over the next 20 years, without any allowance for cost increases.[8]

Similarly, the bridge replacement program, for which Congress authorized $125 million annually in 1971 and 1972, will require large sums. The initial plan calls for an inventory of all bridges on the Federal-aid system; evaluation of their serviceability, safety, and essentiality for public use; and assignment of a priority for replacement of each bridge. Preliminary estimates indicate that, of the 563,000 bridges in the nation, 88,900 are critically deficient, and that 900 new major waterway crossings are needed. Total costs are estimated at $18.8 billion. Nearly three-fourths of the bridges are on country, secondary, and rural roads not affiliated with the Federal-aid highway system.[9]

The needs estimate covers capital expenditure requirements only—i.e., new construction, reconstruction, major resurfacing, and enhancement—and excludes the $18.8 billion said to be needed for bridges. Maintenance and administration expenses are not included. In presenting the needs estimates, the Bureau of Public Roads cited several reasons why the projections probably understate actual current needs: (1) travel projections, particularly in urban areas, have proved too conservative in the past, and seem likely to be so in the latest projections; (2) legislation since the basic estimates were prepared has provided for new programs such as an urban system, relocation housing assistance, and fringe parking; (3) the growing awareness of the social and environmental responsibilities of the highway program calls for new design concepts; and (4) new safety features are not reflected in the projection of needs.[10]

Even with the exclusions noted, this needs estimate implies a level of highway capital outlay, in each of the next 15 years, roughly twice present spending. Drawing board needs, of course, differ from what is technically, politically, or economically feasible to accomplish within a given time span. Existing Federal highway-user taxes, if extended, would yield an estimated $6.6 billion in 1980, only $1.7 billion more than in 1970. State-local highway-user receipts, which support both maintenance and capital expenditure, now amount to $9 billion (excluding bond proceeds) and will rise slowly. Thus within the present financial structure, it seems highly unlikely that such needs estimates could become a realistic policy goal for achievement in the next 15 years.

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8. Address by Federal Highway Administrator F. C. Turner before Northern Virginia Chapter, Virginia Motor Vehicle Conference, September 23, 1971; Arlington, Virginia, U.S. Department of Transportation, Federal Highway Administration *News*, pp. 4–5.
9. *1970 Needs Report*, *op. cit.*, p. 59.
10. *Ibid.*, p. 54.

Projections

The full effect of recent Federal legislation on highway policy remains to be seen, and still other questions concerning future policy are as yet unanswered. What seems clear, however, is that as work on the 42,500-mile interstate system tapers off, there is not likely to be a corresponding decline in highway activity. Numerous other programs seem potential candidates for Congressional consideration. As noted above, the new urban system and the bridge replacement program will require sizable funds if these program goals are to be realized. The Federal Highway Administrator has suggested that the major focus of the post-interstate program should be on cities and the primary road system. The latter system is made up of highways usually signed as U.S. routes (e.g., U.S. 1). One recommendation is that the heaviest traveled of these roads be converted into "Junior Interstates," by building a parallel two-lane road to make divided highways out of them; estimated Federal and state

Table 6.5

Local Expenditures for Highways by Purpose

Actual and Projected, Selected Fiscal Years, 1955–1980

Fiscal year	Total highways	Purpose	
		Current operation	Capital outlay
	Amount (millions)		
Actual:			
1955	$ 6,452	$ 2,215	$ 4,237
1960	9,428	3,088	6,340
1965	12,221	3,897	8,324
1970	16,427	5,665	10,762
Projected:			
1975	22,969	8,209	14,760
1980	29,810	11,402	18,408
	Percent increase, selected intervals		
1955–1960	46	39	50
1960–1965	30	26	31
1965–1970	34	45	29
1970–1975	40	45	37
1975–1980	30	39	25
1960–1970	74	83	70
1970–1980	81	101	71

Source: Actual data from U.S. Department of Commerce, Bureau of the Census. Computations and projections by Tax Foundation.

costs are a minimum of $2 billion annually.[11]

Although illustrative projects have been indicated, no attempt is made here to specify the nature of future highway investment. The projections assume that increases in capital expenditures for highways will parallel those of the past decade, rising somewhat more rapidly in the early part of the seventies and at a slightly slower pace thereafter, following completion of the interstate system. (It is implicitly assumed here that the Highway Trust Fund or an alternate means of Federal financing will be continued past the presently scheduled expiration date in 1977.)

Capital expenditures are estimated at $14.8 billion in 1975 and $18.4 billion in 1980, as compared with $10.8 billion in 1970. For the decade as a whole, the projected annual rate of rise is 5.5 percent, the same as was experienced during the sixties (Table 6.5).

Outlays for current operations—maintenance, administration, and research—are projected to double during the decade, rising from $5.7 billion in 1970 to $11.4 billion in 1980. The accelerated rate, 7.2 percent per year as compared to 6.3 percent in the sixties, is due mainly to sharply rising costs foreseen for maintaining roads and streets.

According to the projections, total highway outlays would rise by about four-fifths, or from $16.4 billion in 1970 to $29.8 billion in 1980. Relative gains would average 6.1 percent annually, as compared to 5.7 percent in the previous decade.

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11. Address by F. C. Turner, Federal Highway Administrator, before Annual Highway Safety Conference of the National Association of Women Highway Safety Leaders, Inc., October 5, 1971, U.S. Department of Transportation, Federal Highway Administration *News*.

VII.
Over-All Expenditures and Related Considerations

This Chapter reviews recent over-all trends in spending, presents projections for the categories not included in the four major functions previously discussed, and summarizes the expenditure projections. At the same time, perspectives on the expenditure totals are provided by comparison of rates of growth over time, and in relation to population and income.

Trends in Over-All Spending

While the expansion of state-local budgets has been remarkably persistent from year to year since 1950, there have been at least three apparent "cycles" of growth, each of intermediate length. These three periods were characterized by different rates of change reflecting underlying social, political, and economic forces at work. The first occurred in the postwar years up to 1960, when states and localities—like other sectors of the economy—were trying to cope with dislocations generated largely by the depression in the thirties and the war in the forties, as well as by changing demographic characteristics. These influences have been documented.[1] In the years from 1950 to 1960 state-local general outlays grew from $23 billion to $52 billion, at average annual rates of around 9 percent. During the same period, growth in the over-all economy, as measured by the gross national product, increased at rates under 7 percent annually.

By the early sixties, the thrust of the forces more or less automatically boosting state-local outlays appeared to have lessened somewhat. Expenditure gains from 1960 to 1965 eased to 7½ percent annually, not so far out of line with increases in other major sectors. (The gross national product rose by a little over 6 percent a year.)

A third "cycle" appears to have gotten under way in the last half of the sixties, ushering in unprecedented increases in outlays of states and localities. Spending rose from $75 billion in fiscal 1965 to $131 billion by 1970, by more than three-fourths. Annual rates of growth averaged 12 percent in this five-year interval, and extended up to 13 and 14 percent in the most recent years reported. By comparison, annual rates of change in other sectors of the economy from 1965 to 1970, seemed modest:[2]

Sector	*Rate (percent)*
Consumer buying	7
Business spending for new plant and equipment	5
Federal government purchases	8
Gross national product	7
State-local purchases	12

1. See, for example, *Fiscal Outlook for State and Local Government to 1975*, Tax Foundation, 1966.
2. Computations based on purchases of goods and services, calendar year basis. Data from Bureau of Economic Analysis, U.S. Department of Commerce.

Table 7.1

Sources of Growth in State–Local General Expenditures

Fiscal Years 1965 to 1970

Source	Annual rate of change (percent)	Percent of total increase	Amount of increase (billions)
Population[a]	1.1	9.1	$ 5.2
Price[b]	3.8	31.7	18.0
Other	7.1	59.2	33.6
Total	12.0	100.0	$56.8

a. Total population growth only.
b. Consumer prices only.
Source: Computed from data published by U.S. Department of Commerce and U.S. Department of Labor.

Available evidence suggests that in the past two years (since the 1970 fiscal year ended) state–local finance has continued as the *number one* growth sector of the economy, although there are indications that recent increases have receded from previous peak rates.

Some of the underlying influences are discussed in Chapter II. While it is not possible to isolate and measure the influence of all causal factors, Table 7.1 summarizes effects of some broad elements. It shows the relative contribution of changes in population and prices generally to the 1965–1970 expansion of state–local outlays.

Within the context of this analysis, it can be seen that factors other than general population and price trends contributed nearly three-fifths ($34 billion) of the increase. This "all other" category includes the effects of program additions and expansions; excess inflation (as through more rapidly rising salaries in government, medical care, construction, etc.); more intensive utilization of state–local services per unit of population; and still other influences.

General price effects, however, were significant, accounting for almost one-third, or $18 billion, of the 1965–1970 rise in state–local spending. General population growth accounted for less than 10 percent, or $5 billion, of the rise.

The Outlook

Previous chapters have dealt with education, public welfare, health and hospitals, and highways. In total these four largest categories account for about 70 percent of state–local general spending. To gain perspective on the entire expenditure outlook, it is first necessary to examine the remainder of categories, accounting for about 30 percent of the total.

Miscellaneous General Expenditures. These other services, classified as "miscellaneous," cover a wide range of somewhat heterogeneous activities. While there was variation in growth rates among the different types of services in this group, the over-all rate of increase in the past decade was similar—only slightly less—than for the four largest categories. From 1960 to 1970 miscellaneous general expenditures rose from $16 billion to $38 billion, or at an average rate of 9.3 percent a year. After adjustment for growth in total population and in general prices, the annual increases during the sixties averaged 5.5 percent; that is to say, the per capita rise in real terms was 5.5 percent a year.[3]

Projections for the six segregable classifications of these miscellaneous

3. "Real," as used here, means that adjustment has been made for consumer prices generally; no account is taken of differential rates which apply to state–local purchases (see discussion in Chapter II).

Table 7.2

Detail of State–Local General Expenditures for Miscellaneous Functions[a]

Actual and Projected, Selected Fiscal Years, 1950–1980

Fiscal year	Function					
	Police and fire	General control[b]	Interest on general debt	Sanitation and sewerage	Housing and urban renewal	All other[c]
	Amount (millions)					
Actual:						
1950	$1,264	$1,041	$ 458	$ 834	$ 452	$ 3,070
1955	1,923	1,452	838	1,142	499	3,819
1960	2,850	2,113	1,670	1,727	858	6,313
1965	3,855	2,773	2,490	2,360	1,250	9,358
1970	6,518	4,682	4,374	3,413	2,138	16,715
Projected:						
1975	10,448	7,402	7,506	8,585	3,585	28,800
1980	16,226	11,340	12,475	11,333	5,826	46,760
	Percent increase, selected intervals					
1950–1955	52.1	39.5	83.0	36.9	10.4	24.4
1955–1960	48.2	45.5	99.3	51.2	71.9	65.3
1960–1965	35.3	31.2	49.1	36.7	45.7	48.2
1965–1970	69.1	68.8	75.7	44.6	71.0	78.6
1970–1975	60.3	58.1	71.6	151.5	67.7	72.3
1975–1980	55.3	53.2	66.2	32.0	62.5	62.4
1960–1970	128.7	121.6	161.9	97.6	149.2	164.8
1970–1980	148.9	142.2	185.2	232.1	172.5	179.7
	Annual rates of change, selected intervals					
1950–1955	8.8	6.9	12.8	6.5	2.0	4.5
1955–1960	8.2	7.8	14.8	8.6	11.4	10.6
1960–1965	6.2	5.6	8.3	6.5	7.8	8.2
1965–1970	11.1	11.0	11.9	7.7	11.3	12.3
1970–1975	9.9	9.6	11.4	20.0	10.9	11.5
1975–1980	9.2	8.9	10.7	5.7	10.2	10.2
1960–1970	8.6	8.3	10.1	7.0	9.6	10.2
1970–1980	9.5	9.2	11.0	12.8	10.5	10.8

a. Totals appear in last column of Table 7.3.
b. Includes financial administration.
c. Excludes education, highways, public welfare, and health and hospitals.
Source: Basic data from U.S. Department of Commerce, Bureau of the Census. Computations and projections by Tax Foundation.

Table 7.3

Summary of State–Local General Expenditures by Major Function

Actual and Projected, Selected Fiscal Years, 1950–1980

Fiscal year	Total general	Major function				
		Education	Highways	Public welfare	Health and hospitals	All other[a]
	Amount (millions)					
Actual:						
1950	$ 22,787	$ 7,177	$ 3,803	$ 2,940	$1,748	$ 7,119
1955	33,724	11,907	6,452	3,168	2,524	9,673
1960	51,876	18,719	9,428	4,404	3,794	15,531
1965	74,546	28,563	12,221	6,315	5,361	22,086
1970	131,332	52,718	16,427	14,679	9,668	37,840
Projected:						
1975	214,800	80,746	22,969	27,128	17,631	66,326
1980	320,021	116,877	29,810	39,460	29,914	103,960
	Percent increase, selected intervals					
1950–1955	48.0	65.9	69.7	7.8	44.4	35.9
1955–1960	53.8	57.2	46.1	39.0	50.3	60.6
1960–1965	44.0	52.6	29.6	43.4	41.3	42.2
1965–1970	76.2	84.6	34.4	132.4	80.3	71.3
1970–1975	63.6	53.2	39.8	84.8	82.4	75.3
1975–1980	49.0	44.7	29.8	45.5	69.7	56.7
1960–1970	153.2	181.6	74.2	233.3	154.8	143.6
1970–1980	143.7	121.7	81.5	168.8	209.4	174.7
	Annual rates of change, selected intervals					
1950–1955	8.2	10.7	11.2	1.5	7.6	6.3
1955–1960	9.0	9.5	7.9	6.8	8.5	9.9
1960–1965	7.6	8.8	5.3	7.5	7.2	7.3
1965–1970	12.0	13.0	6.1	18.4	12.5	11.4
1970–1975	10.3	8.9	6.9	13.1	12.8	11.9
1975–1980	8.3	7.7	5.4	7.8	11.2	9.4
1960–1970	9.7	10.9	5.7	12.8	9.8	9.3
1970–1980	9.3	8.3	6.1	10.4	12.0	10.6

a. See detail in Table 7.2.

Source: Basic data from U.S. Department of Commerce, Bureau of the Census. Computations and projections by Tax Foundation.

functions appear in Table 7.2, along with historical trends. The projections are designed to answer the question: What levels of expenditure would prevail in 1975 and 1980 if per capita spending for each of the functions, in constant dollars, continues to rise at the rate experienced from 1960 to 1970?

According to the projections, outlays for the miscellaneous activities would rise from $38 billion in 1970 to $104 billion by 1980, by 10.6 percent annually.

The fastest growing categories among these miscellaneous functions are seen as sanitation and sewerage; interest on general debt; housing and urban renewal; and "all other." The last grouping includes local parks and recreation, natural resources, airports, water transport and terminals, employment security administration, and general public buildings.

In all cases the increases depicted for the rest of the seventies are somewhat above those of the sixties. The differential is due to the assumption that general prices will rise slightly faster in the period ahead.

Summary of Expenditure Projections

The outlook for total spending by major functions is depicted in Table 7.3, in comparison with historical trends. Under the assumptions behind this study, state and local general expenditures would rise from $131 billion in fiscal 1970 to $215 billion by 1975 and $320 billion by 1980. The ten-year rise to 1980 of 144 percent would be somewhat less than the 153 percent growth in the past decade. In terms of annual rates, the projections indicate a 9.3 percent yearly rise to 1980, compared

Table 7.4

Functional Distribution of State-Local General Expenditures

Actual and Projected, Selected Fiscal Years, 1960–1980

Function	Percent of total				
	Actual			Projected	
	1960	1965	1970	1975	1980
Total general	100.00	100.00	100.00	100.00	100.00
Education	36.08	38.32	40.14	37.59	36.52
Highways	18.17	16.39	12.51	10.69	9.32
Public welfare	8.49	8.47	11.18	12.63	12.33
Health and hospitals	7.31	7.19	7.36	8.21	9.35
Police and fire	5.49	5.17	4.96	4.86	5.07
General control[a]	4.07	3.72	3.56	3.45	3.54
Interest on general debt	3.22	3.34	3.33	3.49	3.90
Sanitation and sewerage	3.33	3.17	2.60	4.00	3.54
Housing and urban renewal	1.65	1.68	1.63	1.67	1.82
Other general	12.17	12.55	12.73	13.41	14.61

a. Includes financial administration.
Source: Computed from data in Tables 7.2 and 7.3.

Table 7.5

State–Local General Expenditures for Major Functions in Relation to Personal Income

Actual and Projected, Selected Fiscal Years, 1960–1980

Function	Expenditures per $1,000 of personal income				
	Actual			Projected	
	1960	1965	1970	1975	1980
Total general	$131.99	$144.82	$169.03	$184.16	$193.68
Education	47.63	55.49	67.85	69.23	70.73
Highways	23.99	23.74	21.14	19.69	18.04
Public welfare	11.20	12.27	18.89	23.26	23.88
Health and hospitals	9.65	10.41	12.44	15.12	18.10
Police and fire	7.25	7.49	8.39	8.96	9.82
General control[a]	5.38	5.39	6.02	6.35	6.86
Interest on general debt	4.25	4.84	5.63	6.44	7.55
Sanitation and sewerage	4.39	4.58	4.39	7.36	6.86
Housing and urban renewal	2.18	2.43	2.75	3.07	3.53
Other general	16.06	18.18	21.51	24.69	28.30

a. Includes financial administration.
Source: Computed from data in Tables 7.2 and 7.3.

to 9.7 percent in the sixties. Higher rates, averaging 10 percent annually, are portrayed in the first of the projection period, gradually slowing to 8 percent in the last part of the decade.

The only factor accounting for the indicated decline in the over-all rate of spending is the expectation that caseloads in education and in welfare will rise less rapidly in the years ahead. For all other services combined (i.e., the total less education and welfare), outlays are shown as rising from $64 billion in 1970 to $160 billion in 1980, or at annual rates averaging 9.6 percent as compared with 8.3 percent in the sixties.

Other Perspectives on the Projections

The projections reveal some shifts as among different functional groupings, as well as further increases above the rise in personal income and population.

Functional Shifts. Some reallocation of funds among the major functions is foretold in the projections, with the role of education and highways in the total declining significantly from recent levels (Table 7.4). The share of the budget devoted to education rose from 36 percent in 1960 to 40 percent in 1970, but is projected to fall back to 37 percent by 1980. The share for highways—18 percent in 1960, fell to 12.5 percent in 1970 and is projected to drop to just over 9 percent by 1980. Further increases in the portion of funds for public welfare, health and hospitals, and most other types of general spending are foreseen by 1980.

Relation to Income. Table 7.5 directs attention to the relationship between

state-local expenditures and personal income. From 1960 to 1970 expenditures rose from $132 to $169 per $1,000 of personal income. The increase in expenditures (153 percent) was nearly three-fifths higher than the 98 percent rise in personal income. The 1980 projections of expenditures amount to $194 per $1,000 of the assumed levels of personal income. All major functions except highways would continue to rise at rates above personal income gains.

Per Capita Changes—Current and Constant Dollars. Data in Table 7.6 provide

Table 7.6
Per Capita State-Local General Expenditures for Major Functions in Current and Constant Dollars
Actual and Projected, Selected Fiscal Years, 1960–1980

Function	Amount				Percent increase[a]	
	Actual		Projected			
	1960	1970	1975	1980	1960–1970	1970–1980
	Current dollars					
Total general	$289	$644	$993	$1,386	123	115
Education	104	259	373	506	148	96
Highways	53	81	106	129	53	60
Public welfare	25	72	125	171	193	137
Health and hospitals	21	47	82	130	124	173
Police and fire	16	32	48	70	101	120
General control[b]	12	23	34	49	95	114
Interest on general debt	9	21	35	54	131	152
Sanitation and sewerage	10	17	40	49	74	193
Housing and urban renewal	5	10	17	25	119	141
Other general	35	82	133	203	133	147
	Constant 1970 dollars[c]					
Total general	$380	$644	$821	$990	70	54
Education	137	259	309	361	89	40
Highways	69	81	88	92	17	14
Public welfare	32	72	104	122	124	69
Health and hospitals	28	47	67	93	71	95
Police and fire	21	32	40	50	53	57
General control[b]	15	23	28	35	49	53
Interest on general debt	12	21	29	39	76	80
Sanitation and sewerage	13	17	33	35	33	109
Housing and urban renewal	6	10	14	18	67	72
Other general	46	82	110	145	78	76

a. Computed on the basis of unrounded numbers.
b. Includes financial administration.
c. Adjusted by consumer price index.
Source: Computed from data in Tables 7.2 and 7.3, with price data from the Bureau of Labor Statistics, U.S. Department of Labor.

perspectives on expenditure trends adjusted for population and general prices. Per capita state-local spending rose from $289 in 1960, by 123 percent, to $644 in 1970. In current dollars, the projections indicate a future rise to $1,386 by 1980, or 115 percent.

In dollars of 1970 purchasing power, per capita state-local outlays would rise by 54 percent from 1970 to 1980, to $990. The increase shown for some services is significantly higher than the over-all average.

Expenditures by Object. The number of (full-time equivalent) employees of state-local jurisdictions is estimated to increase by 2.6 million from 1970 to 1980, of from 8.5 to 11.1 million—a percentage rate significantly below that of the sixties (Appendix Table A.5). The slackening reflects educational trends discussed elsewhere. With average salaries continuing to go up at rates of the 1960–1970 period, however, payrolls would still increase substantially—by 2.4 times as compared to 2.6 times in the sixties.

Capital outlays, in current dollars, are projected as approximately doubling, rising from $30 billion in 1970 to $58 billion in 1980 (Appendix Table A.6). The "money" increase is proportionately about the same as in the sixties. Growth in actual physical volume (*i.e.*, adjusted for prices) would be somewhat less.

Some Uncertainties

Based on trends during the sixties and assumptions concerning future economic parameters, the projections do not take into account future policy decisions which could influence spending. In particular, no allowance is made for the potentially stimulative effect of new funds from the Federal revenue sharing program.[4] Other Federal programs are under consideration (e.g., national health insurance) or have recently been enacted (welfare for adult categories) under which the Federal government would take over the financing and administration of some programs formerly administered by state-local units. There is no way of knowing to what extent any resulting influx of new Federal funds would add to the total stream of spending by all levels of governments, or would serve as a substitute for state-local funds now applied to similar programs.

4. See Chapter VIII, page 93.

VIII.

General Revenues

The rapid growth in state-local spending during the sixties was paralleled by gains in revenue.[1] For the decade as a whole, annual revenue increases averaged 10 percent. As was the case with spending, however, this average obscures the disparate rates of change which took place at different intervals within the period. From 1960 through 1965, the rate of increase was just under 8 percent a year, more than 2 percentage points less than the rate for the preceding five years (1955–1960).[2] This slowing in the revenue growth rate, however, proved to be short-lived. In the ensuing five years increases averaged 12 percent annually and reached 13 and 14 percent in the last two fiscal years reported (1969 and 1970). By 1970, general revenues totaled $130.8 billion, up $80 billion or 159 percent from their 1960 level.

Accompanying these revenue increases were some significant structural changes, as reflected both in intergovernmental financing arrangements and in the composition of revenues raised by state-local units from their own sources. Each of the major revenue sources contributed to the over-all rise—state and local taxes, charges and other nontax revenues,[3] and Federal grants-in-aid. While Federal grants more than doubled, rising faster than other revenue components, $65 billion, four-fifths of the decade's rise in revenues, came from state-local own sources. Substantial though it was ($51 billion), the rise in state-locally imposed taxes lagged proportionately behind that of other major revenue categories, with the result that taxes dropped from around 72 percent of general revenues in 1960 to 66 percent in 1970. Revenues from charges and miscellaneous sources rose from 15 to 19 percent of the total, and Federal grants from 14 to 17 percent.

These broad structural changes were accompanied by other developments leading to a decline in the role of local governments, relative to higher levels, in financing combined state-local services. Shifts in the intergovernmental shares of state-local financing are depicted in Table 8.1, showing general revenues according to the originating level of government. During the decade the rise in funds raised by Federal and state units combined grew at a rate half again as rapidly as that for locally

1. The term "revenue," as used here, deals with "general revenue" only; that is, all state-local revenue except that from utilities, liquor stores, and insurance-trust systems (employee retirement, unemployment and workman's compensation).
2. Data on historical trends appear in Table 8.11, along with projections.
3. Designated as current charges and miscellaneous general revenues, these categories comprise amounts received from the public for performance of specific services benefiting the person charged; from sales of commodities and services except those by liquor stores and local utilities; from fees, toll charges, tuition, gross income of commerical-type activities—parking lots, school lunch programs, etc. Miscellaneous general revenue includes interest earnings on deposits and securities other than interest on insurance trust funds, special assessments, sales of property, and other items.

8.1

Table 8.1

Origin of State–Local General Revenues by Level of Government

Selected Fiscal Years, 1960–1970

Fiscal year	Level of government				Exhibit: local property tax
	Total	Federal	State	Local	
	Amount by originating level (millions)				
1960	$ 50,505	$ 6,974	$20,618	$22,912	$15,798
1965	74,000	11,029	30,610	32,362	21,817
1970	130,756	21,857	57,507	51,392	32,963
	Percentage distribution				
1960	100.0	13.8	40.8	45.4	31.3
1965	100.0	14.9	41.4	43.7	29.5
1970	100.0	16.7	44.0	39.3	25.2
	Hypothetical amounts under 1960 distribution (millions)				
1970	$130,756	$18,044	$53,348	$59,363	$40,927

Source: Basic data from U.S. Department of Commerce, Bureau of the Census. Computations by Tax Foundation.

generated funds. As a result, the amount raised by local governments alone dropped from 45 percent of the total in 1960 to 39 percent in 1970. This shift occurred largely in the last five years of the period. In the absence of this change in intergovernmental shares—and assuming that the same amount of money would have been raised regardless of the level of government responsible for financing—the local share of the total would have been $59 billion in 1970, instead of the $51 billion actually raised. Within this framework of reasoning, revenues raised by localities in 1970 were less by $8 billion, or 13 percent, than under the 1960 sharing arrangements. The states and the Federal government each furnished about $4 billion of this "reduction" in revenue originating locally over the ten-year span.

This shift in intergovernmental financing also appears to have been associated in part with a similar decline in administrative responsibility of local governments relative to the states. State direct expenditures for state functions, for example, grew by 174 percent from 1960 to 1970; local outlays for services administered locally grew by 143 percent. To some extent these different growth rates reflect varying trends in expenditures for services financed primarily by states (e.g., higher education) or by localities (e.g., public schools). In other instances, however, the shift resulted from deliberate takeover of larger shares of administrative responsibility by the states.[4]

4. For example, in 1960 state governments as a whole (then as now there were important variations among individual states) paid directly for about one-half of all public welfare services, with the localities as a group disbursing about the same amount; by 1970, the states spent 25 percent more than localities in direct welfare outlays.

The outlook for future revenues can best be examined through separate analysis of the major components of state-local general revenues—taxes, charges and miscellaneous receipts, and Federal grants-in-aid.[5]

State and Local Taxes

State-local tax collections rose from $36.1 billion in 1960 to $86.8 billion in 1970, by over $50 billion or 140 percent.[6] The annual rate of the increase for the decade as a whole was just over 9 percent. While, as noted earlier, the rise in taxes alone was not proportionately as steep as that for other revenue sources, more than three-fifths of the total revenue increase came from taxes. Year-to-year increments in tax collections were somewhat uneven, reflecting changes in the taxable base brought on by both economic fluctuations and new tax laws. In general, there was a sharp acceleration in the rate of increase beginning in 1966. Prior to that—from 1961 through 1965—annual increments averaged 7.3 percent. In succeeding years of the decade annual increases averaged 11 percent and exceeded 13 percent in 1969 and 1970.

Shifting Tax Sources

Underlying the over-all rise in taxes were disproportionate rates of growth in different tax sources. Gaining most strongly were levies on individual income and general sales, for which yields more than tripled during the decade. These two sources rose half again as rapidly as the total for all other taxes combined. For the most part these changes represented an extension of trends since World War II.

The performance of the property tax, however, veered from the pattern set in the previous postwar years. At the turn of the century the tax brought in about 82 percent of state-local tax yields; this portion declined steadily, reaching 46 percent by 1950. In the face of widespread predictions of further decline in its role, the property tax continued to produce around 46 percent of all state-local tax revenues throughout the fifties, and had dropped only slightly (to 44 percent) in its share of the total by 1965.

In the ensuing years, up to 1970, the property tax portion of state-local taxes dropped to 39 percent. In terms of its contribution to total state-local general revenue (i.e., taxes, plus nontax state-local sources and Federal aid), the decline was even more precipitate (Table 8.1). The share of the property tax in over-all state-local finance dropped from 31 percent in 1960 to 25 percent in 1970. On the basis of the same kind of shifting analysis discussed above, the weight of the property tax thus dropped by about one-fifth during the decade. Other means of financing, in this sense, "reduced" property taxes by some $8 billion below the level they would have attained had they maintained their 1960 role in the over-all state-local revenue structure.

Still another measure of the shifting composition of taxes is shown in Table 8.2, relating changes in tax yields to changes in personal income. The percentage change in tax yields per $1,000 of personal income represents, in effect, the change in taxes adjusted for income growth. These comparisons furnish still another measure of the rising importance

5. Receipts from borrowing are not included in revenues. Debt financing is discussed in Chapter IX.
6. Data on historical trends in tax collections appear in Tables 8.7 and 8.11, along with projections.

Table 8.2

Yields of Major State–Local Taxes in Relation to Personal Income

Selected Fiscal Years, 1955–1970

Tax	Tax yields per $1,000 of personal income			
	1955	1960	1965	1970
Total taxes	$78.74	$91.89	$99.55	$111.71
Individual income	4.15	6.23	7.95	13.92
Corporation income	2.49	3.00	3.75	4.81
Sales and gross receipts	25.63	30.15	33.25	39.02
General	10.36	13.17	15.50	20.76
Selective	15.26	16.98	17.75	18.27
Property	35.99	41.74	43.87	43.83
Other	10.48	10.73	10.73	10.13

Source: Basic data from U.S. Department of Commerce, Bureau of the Census and Bureau of Economic Analysis. Computations by Tax Foundation.

of income taxes and general sales taxes. Property tax yields, when adjusted for income change, rose about 16 percent in the last half of the fifties, 5 percent in the first half of the sixties, and declined slightly in the last half of the sixties.

Annual Fluctuations

While long-term growth considerations are of primary concern in projection studies, annual fluctuations in revenues cannot be discounted as regards their possible influence on long-term yields. An uneven pattern of year-to-year changes in tax yields mirrors the expansion and contraction phases of the business cycle, as well as one-time annual boosts in the level of taxes following periods of heavy legislative tax activity.[7] There appears to be some interaction between these two sets of forces, as when threatened deficits—often reflecting a decline in business activity—are met by statutory enactment of higher taxes. Since few tax measures are of a temporary nature, once in force the higher rates tend to become permanent. Thus short-term cyclical declines evoke legislative initiatives with lasting influence on the long-term level of tax revenues.

Two periods of recession occurred during the sixties: (a) the nine months following a peak in May 1960 and extending through February 1961; and (b) the 12 months from November 1969 to November 1970.[8] Thus for the 105 months from February 1961 to November 1969, the general economy was technically in an expansion phase, although growth during the early years

7. Although absolute growth will continue after the initial year reflecting statutory changes, the percentage rise will decline in following years because of the larger base against which future annual increments are to be compared.

8. Based on National Bureau of Economic Research, Inc. determinations as published in *Business Conditions Digest*, U.S. Department of Commerce, February 1972, p. 110. The dates of the latest contraction are tentative and subject to revision as more information becomes available.

of the sixties was somewhat sluggish. The fiscal years during which the recessionary influences were of greatest duration were 1961 and 1970 (in each of which there were seven months of declining economic activity) and 1971 (when five months of the fiscal year fell within the contraction phase).

As Table 8.3 indicates, tax yields reflected the 1961 downturn. Collections from individual income and general sales taxes appear to have responded immediately, whereas the effect was spread out over several fiscal periods for other types of taxes, and extended to 1963 in the case of the property tax. In part, these results may have been due to the variation in collecting and reporting periods for different kinds of taxes, and for different units of government, primarily at the local level.[9] Unlike later years during the sixties, there was relatively little statutory action increasing taxes from 1960 through 1963.

Peak growth in tax collections generally coincided with the peak year in personal income growth (1969). In that year taxes rose 13.5 percent over the previous year, as income increased by 9.6 percent. Yields in fiscal 1970, however, show no visible effect of the economic slowdown that began in December 1969.[10] Although in part this result may reflect the kind of lags noted in the 1961 recession, in the main it appears that, at least for states, legislative action was taken in advance to

9. For most state governments, and for school districts, the fiscal year is the 12 months ending June 30; among other units of local government, there is more variation in fiscal years, and a considerable proportion use a period ending December 31.

10. The experience was similar in fiscal 1971, when the collections rose by 9.4%.

Table 8.3

Range of Variation in Annual Increases in State-Local General Revenue by Source[a]

Fiscal Years 1961–1970

Revenue source	Low		High		Median percent change
	Year	Percent change	Year	Percent change	
All general revenue	1961	7.0	1970	14.2	9.8
Total, own sources	1963	6.4	1970	14.2	8.8
Total, taxes	1963	5.9	1969	13.5	8.2
Individual income	1961	6.1	1968	25.4	16.3
Corporation income	1962	3.3	1969	26.3	12.8
General sales	1961	4.9	1969	20.6	11.0
Selective sales	1962	5.4	1970	13.7	7.0
Property	1963	4.1	1970	11.0	6.8
Other taxes	1962	3.2	1968	11.3	6.2
Charges and miscellaneous	1961	8.5	1970	18.3	11.2
Federal grants-in-aid	1961	2.3	1966	19.8	11.6
Exhibit: personal income	1961	3.4	1969	9.6	7.6

a. Percentage changes over previous fiscal year.
Source: U.S. Department of Commerce, Bureau of the Census, and Tax Foundation computations.

Table 8.4

Legislative Actions Increasing Major State-Level Taxes

January 1, 1959 through January 1, 1972

Tax	Number of legislative actions			Number of states levying tax, 1972
	Total	Increasing tax rates	Enacting new taxes	
Total	514	474	40	—
General sales	75	63	12	45
Personal income	66	54	12	40[a]
Corporation income	71	62	9	44
Motor fuels	71	71	—	50
Cigarette	145	140	5	50
Alcoholic beverages	86	88	2	50

a. Excludes Connecticut, New Hampshire, and Tennessee, where tax applies to certain investment income only; and New Jersey, where tax applies to commuters' income only.

Source: Advisory Commission on Intergovernmental Relations (1959-1970) and Tax Foundation records (1971).

ward off budget deficits which would otherwise have resulted from the threatened decline in taxes below amounts anticipated when budgets were drawn up, sometimes as long as 18 to 30 months in advance of a fiscal period. Legislative action in 1969 and 1971 set new records in statutory tax increases.

Just as legislative decisions and economic change interacted in shaping short-run fluctuations in tax receipts, these factors were the major source of long-term growth in tax revenues during the sixties.[11]

Legislative Tax Increases

Statutory revisions in state taxes were extensive during the sixties. Table 8.4 presents the record of new tax enactments and rate increases for the six major state tax sources during the period from 1959 to January 1, 1972. During this period there were 40 adoptions of a major state tax, and a total of 474 rate increases in existing taxes.

The annual volume of state tax-raising measures was especially heavy in recent years. New records of $4 billion and $5 billion annually were set in 1969 and 1971, respectively.[12] On the whole, state and local combined taxes in fiscal 1970 were about $13 billion—more than one-third—higher than the yields which would have resulted from the 1965 tax structure without statutory increases.[13]

With these legislative increases, the top rates imposed on the major tax

11. Changes in administrative and collection procedures (e.g., withholding of personal income taxes) also played some part in augmenting tax collections from existing levies; the quantitative importance of such procedural devices, however, is not readily ascertainable, and on the whole is probably relatively small in comparison with the two major growth sources.
12. "State Tax Prospects, 1972," Tax Foundation's *Tax Review*, Vol. 33, No. 3 (March 1972). State tax action is reviewed annually in a fall issue of the *Tax Review*.
13. This $13 billion reflects initial yields generated by new legislation, together with subsequent growth affecting the base to which the new measures were applied. It is based on the difference between the amount the 1965 tax structure would have produced in response to economic change alone and actual tax receipts in 1970.

sources moved up sharply (Table 8.5). General sales tax rates rose from a maximum of 4 percent in 1960 to 7 percent in 1972, top marginal rates on personal income from 10½ to 18 percent, and top corporate income tax rates from 9½ to 12 percent. Similarly, new breakthroughs occurred in the rates of the selective sales taxes. By the end of 1971, the large majority of states had adopted all of the major state taxes.

There is no comprehensive record available as to statutory action on local taxes, particularly the property tax, which makes up 85 percent of local tax revenues. Altogether there were 82,319 local jurisdictions with property-taxing power in 1962; the number declined to 70,726 by 1967, the latest year reported.[14] During the corresponding interval, the market value of locally assessed real property rose from $969 billion to $1,277 billion, or 32 percent (see Appendix Table A.7). At the same time (from fiscal 1962 to fiscal 1967) total property tax collections increased 38 percent. This relationship suggests that legal rate increases in this latest Census period were on the order 1 percent annually.[15] While comparable data are lacking for later years, the performance of the property tax in relation to income in the period from 1965 to 1970 suggests that there has been little, if any, over-all increase in effective property tax rates in relation to income.

For local nonproperty taxes, the major legislative development during the sixties was toward more general use of local sales taxes. Twelve states approved local sales tax levies from 1960 to 1970, bringing the number of jurisdictions

14. *Census of Governments*, Volume 1, 1962 and 1967, Bureau of the Census, U.S. Department of Commerce. The decline reflects mainly a reduction in the number of school districts from around 35,000 in 1962 to 22,000 in 1967, partly offset by a rise in special districts. Not all of these latter districts, however, have taxing powers.

15. This estimate, however, is somewhat tenuous. There are no separate data on the personalty and realty components of property tax collections; and the market values of property as estimated by the Bureau of the Census do not extend to personal property. The net assessed value of personal property, which comprised 14% of the taxable base in 1966, grew only 13% between 1961 and 1966; the corresponding rise in net assessed value of real property was 40%. *Ibid.*

Table 8.5

Illustrative Trends in Statutory Rates of Selected State Taxes, 1960–1972

Tax	Highest state rate		Lowest state rate	
	1960	1972	1960	1972
General sales (percent)	4	7	2	2
Personal income—top marginal rate (percent)	10.5	18	3	2[a]
Corporation income—top marginal rate (percent)	9.5[a]	12[a]	1.75[a]	2.3[a]
Gasoline (cents per gallon)	7	10	3	5
Cigarette (cents per pack)	8	21	2	2

a. Applies to all taxable income.
Source: State Tax Guide, Commerce Clearing House.

Table 8.6

Income Elasticity of Major State–Local Taxes[a]

Tax	Range in other studies[b]	As projected in this study
Individual income	1.5–1.8	1.7
Corporate income	1.1–1.3	1.2
Property	.7–1.1	.9
General sales	.9–1.05	1.1
Motor fuels	.4– .6	.6
Tobacco	.3– .4	.5
Alcoholic beverages	.4– .6	.5
Other selective sales	.9–1.1	.9
Motor vehicle licenses	.2– .4	.5
All other	.6–1.2	.9

a. Percent change in tax yield per 1 percent change in gross national product.

b. These are elasticities derived in more than a dozen studies. See *Federal-State Coordination of Personal Income Taxes*, Advisory Commission on Intergovernmental Relations, Washington, October 1965, p. 42, for a list of authors.

levying the tax to more than 3,500, located in 24 states and the District of Columbia. In contrast, the trend toward wider use of local income taxes was more restrained. The major new adoptions of local income taxes were in Michigan, where the state authorized a uniform city income tax in 1964, and in New York City and Baltimore. By 1970 income or payroll levies were being utilized by several thousand localities in nine states and the District of Columbia.[16]

Projections—Taxes

Given the previously stated assumptions concerning the course of the economy and the automatic response of different taxes to economic growth, it is now possible to project future yields from the 1970 tax structure.[17] Table 8.6 presents data on the typical performance of each major tax when income rises by one percent.[18]

If the present tax system were left to itself, without increases in statutory rates or the adoption of new levies, what amounts would be available in 1975 and 1980? The results, and some perspectives on them, appear in the accompanying tables.

Total taxes would rise to around $201 billion by 1980, about 2.3 times their size in 1970 (Table 8.7). The rate of advance would be only slightly less than that experienced during the sixties. It should be noted, however, that increases would be somewhat higher—around 10 percent annually—during the early part of the period, falling to around 7.5 percent in the latter part of the decade.[19]

16. For a discussion of the historical development, revenue effects, and other characteristics of local sales and income taxes, see *City Income Taxes* (1967) and *State and Local Sales Taxes* (1970), published by the Tax Foundation.

17. As noted below, the projections are adjusted for a portion of the state tax changes enacted in 1971. According to the assumptions as spelled out in Chapter II, gross national product would rise by 55.0% in current dollars, from 1970 to 1975 and by 41.7% from 1975 to 1980. Real output is computed as rising at 4.1% annually from 1969; prices are assumed to rise at the rate of 3.9% from 1970 to 1975 and 3.0% from 1975 to 1980.

18. Total yield from a given tax structure over a period of time will reflect economic change according to the shifting weight of each tax. The automatic response of tax yields to income change, plus new tax legislation during the sixties, combined to raise the over-all income elasticity of state–local taxes from .91 in 1960 to .98 by 1970. Without further legislation, this measure would rise to around 1.07 by 1980. That is to say, for each 10 percent change in income, tax revenues would rise by 10.7 percent. A fuller discussion of elasticities for various taxes was given in *Fiscal Outlook for State and Local Government to 1975*, Tax Foundation, New York, 1966, pp. 103–106.

19. Two technical characteristics of the projections methodology produce this result: (a) the inclusion of some $4.4 billion annually in tax increases enacted since the end of the 1970 fiscal period (up to October 1971), which have already raised potential yields in 1975; and (b) the assumption of a leveling in general price increases in the latter part of the seventies. (The tax projections do not take into account an additional $1.5 billion annually in higher state taxes enacted in late 1971 and in 1972.)

The outlook would be for a continuation of more intensive use of income taxes, stability in general sales tax shares, and further declines in the role of selective sales, property, and miscellaneous taxes. The property tax, although its role in the structure would decline further, would continue to be by far the largest single tax source, with yields of around $50 billion by 1975 and $70 billion by 1980. No separate projections are made as regards taxes originating at state versus local levels. It is implicit in the projected yield pattern, however, that further increases would occur in the state share of all taxes.

Per capita state-local tax collections would double, rising from $426 in 1970 to $871 in 1980, or 7.4 percent annually. When adjusted for assumed price changes, the per capita increase would be 4.6 percent annually. Total taxes would rise by about $10 per $1,000 of personal income (see Table 8.8).

Table 8.7

Yields of Major State–Local Taxes by Type of Tax[a]

Selected Fiscal Years, 1950–1980

Fiscal year	Type of tax					
	Individual income	Corporate income	Sales: General	Sales: Selective	Property	All other
	Amount (millions)					
Actual:						
1950	$ 788	$ 593	$ (b)	$ (b)	$ 7,349	$ 2,030
1955	1,237	744	3,090	4,553	10,735	3,125
1960	2,463	1,180	5,177	6,672	16,405	4,220
1965	4,090	1,929	7,981	9,136	22,583	5,521
1970	10,812	3,738	16,128	14,194	34,054	7,869
Projected:						
1975	24,243	6,749	26,949	19,824	50,911	11,633
1980	41,435	10,124	39,319	25,108	70,003	15,113
	Percent of total					
1950	5.0	3.7	(b)	(b)	46.2	12.8
1955	5.3	3.2	13.2	19.4	45.7	13.3
1960	6.8	3.3	14.3	18.5	45.4	11.7
1965	7.9	3.7	15.6	17.8	44.4	10.7
1970	12.5	4.3	18.6	16.4	39.2	9.1
1975	17.3	4.8	19.2	14.1	36.3	8.3
1980	20.6	5.0	19.6	12.5	34.8	7.5

a. See total tax collections in Table 8.11. Projections include additions since 1970 up to October 1971: $5,948 in 1975, and $8,922 in 1980. Exclude higher state taxes enacted in late 1971 and in 1972, estimated to yield $1.5 billion per year currently.

b. Detail not available. Total for general and selective sales tax was $5,154 or 32.4 percent of total tax revenue.

Source: Basic data from U.S. Department of Commerce, Bureau of the Census. Computations and projections by Tax Foundation.

Table 8.8

State–Local Tax Collections in Relation to Population and Income[a]

Selected Fiscal Years, 1950–1980

Fiscal year	Per capita[b]		Per $1,000 of personal income
	Current dollars	Constant 1970 dollars	
Actual:			
1950	$105	$170	$ 73.21
1955	143	207	78.73
1960	201	264	91.89
1965	265	327	99.55
1970	426	426	111.71
Projected:			
1975	649	563	120.29
1980	871	668	121.71

a. Excludes social insurance taxes. Constant dollar figures adjusted by consumer price index.

b. Based on estimated total population, including armed forces abroad, at the middle of the fiscal year.

Source: Basic data from U.S. Department of Commerce and U.S. Department of Labor. Computations and projections by Tax Foundation.

These are the results which would occur if the present tax structure were left to itself and if this study's assumptions prove correct as regards the performance of the economy and the rate of inflation. Revenues from existing taxes could be higher or lower than projected, depending upon the *true* course of the economic variables. For a number of reasons, however, it seems highly improbable that the present tax structure will remain unchanged throughout the seventies. For example, as noted earlier, the threat of budget deficits in periods of recession often induces the states to enact new and higher taxes.[20]

Future policy changes—apart from economic conditions—will play a decisive role in determining the actual amounts raised in taxes. Since spending and taxing go hand in hand, a crucial factor will be decisions as to how much of the nation's resources is to be allocated to the state–local sector. The structure of state–local taxes will also be influenced by future decisions concerning the levels of government, and the specific tax sources, from which funds will be raised.

At present major questions as to future tax structures are posed by issues in intergovernmental finance. There are already proposals under active consideration in several states for massive changes in tax structures growing out of recent court decisions questioning the use of the property tax in its present form for the support of public schools. The main thrust of these proposals is to shift more of the tax burden upward to the state level and to substitute state-level taxes for a portion of local taxes on residential property. (See discussion in Chapter III, page 36.) Actions by the legislators and voters up to late 1972 suggest that the states will be slow to approve major changes in their present school financing arrangements unless forced to do so by the courts.

Other General Revenue from State–Local Sources

States and localities in 1970 collected some $22 billion in current charges and fees and miscellaneous general revenues—an amount just slightly in excess of Federal grants-in-aid for the same year. During the sixties revenues

20. While the projections are based on the assumption that there will be no major periods of "depression" during the rest of the seventies, recessionary periods similar to those of the postwar period are not ruled out.

from these state–local sources increased from about 15 to 17 percent of all general revenues.

Charges and fees produced close to $15 billion in fiscal 1970, almost three times as much as in 1960, primarily from users of services in the fields of education, highways, hospitals, housing and urban renewal, and sanitation. Table 8.9 presents receipts from these sources, as related to associated expenditures. Except for the housing and urban renewal category, it appears that charges and fees are being relied on more heavily than in earlier years for financing major services.[21]

Projections—Other General Revenue

The projections assume a continued slight upward drift in the role of user charges and fees, primarily in highway charges, hospital fees, and sanitation services. While user receipts in education (mainly tuition and fees in higher education, but also such items as school lunch sales) moved up in their support of educational outlays in the early sixties, in recent years they have leveled off at around 11 percent of the total. This constant percentage is applied in the projections. Under these assumptions, revenues from charges and fees would reach $26 billion by 1975 and around $40 billion by 1980, increasing by 166 percent for the decade.

A relatively small category of state–local revenue—"miscellaneous general"—displayed the highest growth rate of any major revenue category during the sixties as a whole, and more than doubled during the period from 1965 to 1970 alone. This grouping consists largely of income from special assessments, sale of property, and interest earnings. In part this unusual spurt of growth seems due to conditions not likely to remain permanent; hence some slowing of further increases is projected, with receipts estimated at $13 billion in 1975 and $21 billion in 1980.

Federal Grants-in-Aid

Revenues from Federal grants continued as one of the fastest growing segments of state–local receipts during the sixties, and the increasing trend was accelerated in the years from 1965 to 1970. Federal aid provided under $7 billion of state–local general revenues in 1960 and almost $22 billion in 1970. Annual increases averaged 10 percent in the first half of the sixties and 15 percent in the second half. Table 8.11 depicts these aids as defined by the Census Bureau under intergovernmental revenues to states and localities.

Changes in the functional composition of Federal payments to states and localities are shown in Table 8.10.[22] In all major categories except highways, Federal payments to states and localities have risen significantly as a share of state–local outlays for the same functions. The effects of the introduction of new programs in education and public

21. For a fuller discussion of such charges for cities, see *Special Assessments and Service Charges in Municipal Finance*, Tax Foundation, 1970.

22. The series on Federal intergovernmental expenditures to state–local governments differs somewhat from data published by the Bureau of the Census on revenues from this source as reported by state–local units, as well as from the concept of grants as shown in the Federal budget. Bookkeeping and timing procedures apparently introduce differences in the two series as reported by the Census Bureau. Major differences between the Budget and Census series on Federal payments result from substantive differences in definition of aids. For a full discussion, see *Special Analyses of the United States Government*, Fiscal Year 1973, p. 250.

Table 8.9

State-Local Revenues from Charges and Fees, by Major Function

Selected Fiscal Years, 1955–1980

Fiscal year	Total—all functions	Education	Highways	Hospitals	Housing and urban renewal	All other[b]
	Amount (millions)					
Actual:						
1955	$2,927	$ 939	$ 274	$ 453	$ 269	$1,037
1960	5,319	1,769	568	883	339	1,760
1965	8,402	3,193	700[a]	1,372	458	2,679
1970	14,873	5,803	1,105	3,053	589	4,323
Projected:						
1975	25,729	8,882	1,649	6,841	1,144	7,213
1980	39,500	12,856	2,275	11,607	1,815	10,947
	Percent of expenditures for associated function					
1955	8.8	7.9	4.2	22.1	53.9	8.1
1960	10.3	9.4	6.0	27.3	39.5	9.0
1965	11.3	11.2	5.7	30.3	36.6	9.6
1970	11.3	11.0	6.7	31.6	27.5	12.1
1975	12.3	11.0	7.2	38.8	31.8	12.5
1980	12.8	11.0	7.6	38.8	31.8	12.5

a. Estimated. Data are available for toll facilities only.
b. The largest sources of charges and fees not shown separately here are sanitation and nonhighway transportation.

Source: Basic data from U.S. Department of Commerce, Bureau of the Census. Computations and projections by Tax Foundation.

welfare (e.g., Medicaid) were particularly pronounced in the last part of the sixties.

Although amounts of "aid," as defined by different agencies vary,[23] there can be no doubt by almost any measure that sharp increases in grants occurred in fiscal 1971 and 1972. The latest Federal budget reported a 25 percent rise in grant payments in fiscal 1971, to a level of $29.8 billion, and estimated that the totals would rise to $39 billion in 1972 and further to $43 billion in fiscal 1973.[24]

Congressional action in 1972 will have significant influence on the future course of Federal grants to states and localities. Three enactments, in particular, deserve mention:

1. State and Local Fiscal Assistance Act of 1972. More commonly known as Revenue Sharing, this law provides for the distribution of $30.2 billion over a

23. See note 22 *supra*.
24. *Special Analyses*, *op. cit.*, p. 245. These estimates include $2.25 billion in fiscal 1972 and $5 billion in 1973 for general revenue-sharing.

five-year period, beginning January 1, 1972. Recipients will be more than 38,000 general-purpose state and local governments. (See Appendix III for a summary of provisions.)

2. Federal Water Pollution Control Act Amendments of 1972. This "clean air" law authorized $24.6 billion in 75-percent Federal matching funds, primarily for the construction of municipal waste treatment plants (including sewage collections systems), and to reimburse municipalities for plants they have already built in expectation of Congressional action. Of the $18 billion earmarked for new municipal plants, $5 billion was to be available in fiscal 1973, $6 billion in 1974, and $7 billion in 1975. Previously the Federal matching share of water-pollution projects was 55 percent.

3. Social Security Amendments of 1972. These provisions (discussed in Chapter IV, page 54) will have primary effects in freeing up some state-local funds rather than in affecting the size of future grants.

Projections—Federal Aid

The projections are based on the assumptions that (1) Federal grants for purposes other than general revenue sharing and municipal waste treatment will rise commensurately with associated expenditures for each function (as projected independently); (2) general revenue sharing grants will amount to $6.2 billion in 1975, as now legislated,

Table 8.10

Federal Grants-in-Aid to State-Local Governments by Major Function[a]

Selected Fiscal Years, 1950–1970

Fiscal year	Total—all functions	Education	Highways	Public welfare	Housing and urban renewal	Health and hospitals	Other
	Amount (millions)						
1950	$ 2,371	$ 369	$ 429	$1,131	$ (b)	$ (b)	$ 442
1955	3,099	521	589	1,429	(b)	73	487
1960	6,994	950	2,905	2,070	226	135	708
1965	11,062	1,677	3,997	3,098	676	292	1,322
1970	23,257	5,844	4,608	7,574	1,609	931	2,691
	Percent of state-local expenditures for aided function						
1950	10.0	5.1	11.3	38.5	(b)	(b)	4.9
1955	9.2	4.4	9.1	45.1	(b)	2.9	6.1
1960	13.5	5.1	30.8	47.0	26.3	3.6	4.8
1965	14.8	5.8	32.7	49.1	54.1	5.4	6.3
1970	17.7	11.1	28.1	51.6	75.3	9.6	7.5

a. This series represents Federal intergovernmental expenditures to states and localities and differs somewhat from reported data on intergovernmental revenues received from the Federal government, as shown in Table 8.15.

b. Not available; included in "other."

Source: U.S. Department of Commerce, Bureau of the Census, and Tax Foundation computations.

Table 8.11

Summary of State-Local General Revenue by Major Source

Actual and Projected, Selected Fiscal Years, 1950–1980

Fiscal year	Total general revenue	General revenue from own sources				Federal grants-in-aid
		Total	Taxes	Current charges	Miscellaneous general revenue	
	Amount (millions)					
Actual:						
1950	$ 20,911	$ 18,425	$ 15,914	$ (a)	$ (a)	$ 2,486
1955	31,073	27,942	23,482	2,972	1,487	3,131
1960	50,504	43,530	36,117	5,319	2,095	6,974
1965	74,000	62,971	51,243	8,402	3,327	11,029
1970	130,756	108,898	86,795	14,873	7,230	21,857
Projected:						
1975	227,632	179,233	140,309	25,729	13,195	48,399
1980	329,011	262,057	201,102	39,500	21,455	66,954[b]
	Percent increase, selected intervals					
1950–1955	48.6	51.6	47.6	—	—	25.9
1955–1960	62.5	55.8	53.8	79.0	40.9	122.7
1960–1965	46.5	44.7	41.9	58.0	58.8	58.1
1965–1970	76.7	72.9	69.4	77.0	117.3	98.2
1970–1975	74.1	64.6	61.7	73.0	82.5	121.4
1975–1980	44.5	46.2	43.3	53.5	62.6	38.3
1960–1970	158.9	150.2	140.3	179.6	245.1	213.4
1970–1980	151.6	140.6	131.7	165.6	196.7	206.3
	Annual rates of change, selected intervals					
1950–1955	8.3	8.7	8.1	—	—	4.7
1955–1960	10.2	9.3	9.0	12.3	7.1	17.4
1960–1965	7.9	7.7	7.3	9.6	9.7	9.6
1965–1970	12.1	11.6	11.1	12.1	16.8	14.8
1970–1975	11.7	10.5	10.1	11.6	12.8	17.2
1975–1980	7.7	7.9	7.5	9.0	10.2	6.7
1960–1970	10.0	9.6	9.2	10.8	13.2	12.1
1970–1980	9.7	9.2	8.8	10.3	11.5	11.8

a. Detail not available. Total for current charges and miscellaneous general revenue was $2,511 million.
b. Projections assume the continuation of revenue-sharing beyond the 1976 expiration date in current law. See Appendix I.

Source: Basic data from U.S. Department of Commerce, Bureau of the Census. Computations and projections by Tax Foundation.

Table 8.12

Percentage Distribution of State–Local General Revenue by Major Source

Selected Fiscal Years, 1950–1980

Fiscal year	Total all sources	From own sources			From Federal grants
		Total own sources	Taxes	Other[a]	
Actual:					
1950	100.0	88.1	76.1	12.0	11.9
1955	100.0	89.9	75.6	14.4	10.1
1960	100.0	86.2	71.5	14.7	13.8
1965	100.0	85.1	69.2	15.8	14.9
1970	100.0	83.3	66.4	16.9	16.7
Projected:					
1975	100.0	78.7	61.6	17.1	21.3
1980	100.0	79.6	61.1	18.5	20.4

a. Charges and fees and miscellaneous.
Source: Computed from data in Table 8.11.

and that new legislation will continue these grants at a level of $6.4 billion in 1980; and (3) anti-water pollution grants will be spaced out over a period of years, as construction takes place, totaling $3.5 billion in 1975 and $4.0 billion in 1980.

Based on these assumptions, Federal grants-in-aid would amount to $48 billion in 1975 and around $67 billion in 1980. The rise for the decade would be at approximately the same rate as in the period from 1960 to 1970, but would represent a slowing of recent trends.

Projections of Total General Revenues

Table 8.11 brings together the figures on general revenues—from taxes, charges and miscellaneous sources, and Federal grants-in-aid. General revenues in total are projected as rising from around $131 billion in 1970 to $228 billion by 1975 and $329 billion by 1980, or 2½ times, and slightly less than during the previous decade. The role of state–local taxes would continue to decline somewhat (from 66 percent of the total in 1970 to 61 percent in 1980), as both Federal aids and nontax sources rose in importance (Table 8.12).

IX.

Over-All Finance

In the preceding chapters projections for all general revenues and expenditures have been developed. Table 9.1 presents data on the state of balance on general state–local transactions as projected, with past comparisons. Under the conditions assumed, general revenues would tend to rise at a faster rate than the indicated growth in expenditures. Revenues as projected would exceed spending by around $13 billion in 1975 and $9 billion in 1980, or by 6 percent and 3 percent respectively. While the margins as projected are not large, those of even this magnitude would be unusual for the general accounts.[1] The only year during the sixties in which general revenues exceeded general expenditures was fiscal 1966, when the "surplus" was about two-tenths of one percent. In all other

1. On a national income and product accounts basis, taking into account a more inclusive set of transactions, state–local budgets have produced a surplus in all but three years since 1960. The surplus generally results from an excess of receipts over outlays in social insurance transactions (e.g., employee retirement). (See Appendix Table A.9.) The reported over-all surplus in the second quarter of 1972, however, is so large ($14.8 billion annual rate) as to suggest that there was also a general accounts surplus, excluding social insurance funds.

Table 9.1

Comparison of State–Local General Revenues and General Expenditures

Actual and Projected, Selected Fiscal Years, 1950–1980
(Billions)

Fiscal year	General revenue	General expenditures	Deficit (−) or surplus (+) on general transactions
Actual:			
1950	$ 20,911	$ 22,787	−$ 1,876
1955	33,724	31,073	+ 2,651
1960	50,505	51,876	− 1,372
1965	74,000	74,546	− 546
1966	83,036	82,843	+ 193
1967	91,197	93,350	− 2,153
1968	101,264	102,411	− 977
1969	114,500	116,728	− 2,228
1970	130,756	131,332	− 576
Projected:			
1975	227,632	214,800	+ 12,832
1980	329 011	320,021	+ 8,890

Sources: Tables 7.3 and 8.11.

years there were small deficits on general accounts ranging from four-tenths of one percent (1970) to 2 percent (1967).

The main reason why general accounts are usually in a deficit position is that there is a long-standing tradition in most states and localities of financing sizable portions of capital outlay by borrowing,[2] and some use is made of short-term borrowing. The proceeds from such loans are not considered as "revenue," and are thus not included in Bureau of the Census figures on revenues. Moreover, the retirement of debt issues does not enter as an "expenditure."

Because of debt-financing and for still other reasons, it is necessary to delve further into the financial operations of state–local units before evaluating the adequacy of funds for financing general functions. In addition to debt financing, the other main factors are: (1) states and localities can be expected to increase their holdings of cash and securities both as offsets to debt and as working capital, as their scale of operations expands; and (2) there are claims against general funds (and/or borrowing) to finance some activities not covered under general expenditures.

This section will explore the broader outlook for state–local finance, taking into account fund requirements in addition to those for general expenditures. Particular attention will be given the largest of these sources of demand for added funds—debt transactions.

Debt Transactions

The growth in state–local debt generally kept pace with the rise in revenues and expenditures over the past two decades, increasing from $24 billion in 1950 to $144 billion in 1970, about six-fold.[3] The timing of the growth in debt within the period, however, was notably different from that of other financial aggregates. The most pronounced expansion in debt came from 1950 to 1960, when the volume of outstanding debt almost tripled, reaching $70 billion. In contrast, revenues and expenditures scarcely more than doubled during that interval. The period was marked by an upsurge in capital investment for new schools, roads and streets, buildings, etc.—and the filling of backlogs built up in prior years during the depression and World War II. This pattern was reversed in the years from 1960 to 1970, when the rise in debt (105 percent) was below that for general revenues and expenditures (more than 150 percent).

Moreover, during the last half of the sixties there was no general acceleration in the rate at which debt was increasing, contrary to the sharp jump in the rate of expansion of both revenues and expenditures. Although there were some temporary disturbances in credit markets affecting the rate at which new securities were issued in 1970, a major factor in the relatively stable growth of debt during the sixties appears to have been the lessening in pressures for higher spending for capital improvements.

Apart from the differences in the rate of growth in total debt over the postwar period, there were some notable changes in its composition. Long-term debt

2. Capital outlays of these units totaled $220 billion in the ten years 1961 through 1970. Approximately half of this spending was financed by long-term security issues.
3. Historical data appear in Table 9.3, along with projections.

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declined relatively to the total, as a marked upsurge appeared in outstanding short-term obligations during the last half of the sixties, reflecting in part credit conditions with primary effects on issuance of long term bonds.[4] Another significant turn-around affecting the structure of state–local debt was the reduction in the rate at which nonguaranteed debt was increasing. From 1950 to 1960 this type grew by almost eight-fold; from 1960 to 1970 nonguaranteed debt increased far less, by 123 percent (Appendix Table A.10).

The future demand for credit on the part of the states and localities may be expected to reflect prevailing judgments by those who make the decisions as to the need for capital funds measured against the cost of acquiring them, including the added cost of carrying credit.

Cost of Credit

Forces largely outside the control of state–local units determine the supply of loanable funds in the capital markets and the terms and conditions under which they may be available to borrowers at large. High and rising interest rates tend to reduce current municipal bond sales for a number of reasons: (a) the higher rates add to the cost of the anticipated capital investment and may thus price the asset out of line with expected benefits; (b) when rates are rising, there may be a tendency to postpone borrowing in the hope that rates will fall; and (c) there are legal limitations, in most jurisdictions, on allowable interest rates.

Credit market conditions had strong negative influence on the rate at which municipal bonds were issued during the fiscal year ending June 30, 1970.[5] A tightening in money and credit markets which had been developing for some time became particularly acute in the last half of calendar 1969 (first half of fiscal year 1970). Interest rates on state–local bonds, as well as private issues, rose sharply, with pronounced effects on the timing of bond sales. Studies by the Federal Reserve Board have attempted to measure the effects of the difficulties associated with high interest rates, compounded by legal ceilings on interest rates. The results indicate that restrictive monetary conditions and high interest rates led to a net shortfall of $5.2 billion in long-term borrowing below planned levels for fiscal 1970.[6] State–local units "planned" to borrow $18.5 billion; only $13.3 billion was actually borrowed.

In fiscal 1971, despite various legal and technical problems,[7] state–local units, stimulated by relatively favorable market conditions, issued long-term bonds in record volume. The total, $23.1 billion, represented a sizable

4. Long-term obligations are those with maturity of more than one year; in 1970 they accounted for over nine-tenths of total outstanding debt.
5. High interest rates in calendar year 1966 also had some effect on state–local bond offerings. For an account, see Paul F. McGouldrick, "Monetary Restraint and Borrowing and Spending by Large State and Local Governments in 1966," *Federal Reserve Bulletin*, July 1968; and John E. Peterson, "Monetary Restraint, Borrowing, and Capital Spending by Small Local Governments and State Colleges in 1966," *Federal Reserve Bulletin*, December 1968.
6. A total of $7.4 billion in long-term borrowing setbacks was experienced during the fiscal year; but $2.2 billion, though postponed, was completed before the end of the fiscal year. John E. Peterson, "Response of State and Local Governments to Varying Credit Conditions," *Federal Reserve Bulletin*, March 1971, pp. 209–224.
7. These included voter rejections of 40 percent of proposed borrowing authorizations submitted to a vote; uncertainty over certain Internal Revenue Service guidelines; and questions of constitutionality of a two-thirds majority required for a bond authorization in some jurisdictions. Paul Schneiderman, "Planned and Actual Long-Term Borrowing by State and Local Governments," *Federal Reserve Bulletin*, December 1971, pp. 977–982.

Table 9.2

Capital Outlays and Proceeds of New State–Local Security Issues

Actual and Projected, Selected Years, 1960–1980

Year	Amount (millions)		Percentage financed by borrowing
	Capital outlay	Security issues[a]	
Actual:			
1960	$15,104	$ 7,247	48.0
1961	16,091	9,463	52.6
1962	16,791	8,568	51.0
1963	17,638	9,151	51.9
1964	19,087	10,201	53.4
1965	20,535	10,471	51.0
1966	22,330	11,303	50.6
1967	24,233	14,643	60.4
1968	25,731	16,489	64.1
1969	28,240	11,838	41.2
1970	29,650	18,110	61.1
Projected:			
1975	43,099	25,859	60.0
1980	57,909	34,745	60.0

a. Excludes refunding issues; issues for new capital only.

Source: Capital outlays from Appendix Table A.6; new security issues from Board of Governors of the Federal Reserve System. Computations and projections by Tax Foundation.

increase over the $13.3 billion borrowed in 1970. Although there were some shortfalls below planned levels in the early part of fiscal 1971, most issues were reinstated by the end of the fiscal year, and the *net* borrowing shortfall (i.e., below "plans") was only $0.7 billion, one-third of which was interest-related. Thus it would appear that the volume of municipals in fiscal 1971 fulfilled the pent-up borrowing needs created when some $5 billion in proposed borrowing was rationed out of the market in fiscal 1970.

While the cost of borrowing by states and localities was rising markedly over earlier levels, other issuers of securities were similarly affected. There is no general indication that the quality of state–local bonds deteriorated relative to other issues. Muncipals maintained a favorable interest differential in relation to corporate bonds; although the spread narrowed somewhat (in percentage terms) during the peak of the credit crunch—in 1969 and 1970—the previous differential had been restored by 1971.

There also appears to have been no apparent worsening in the ability of states and localities to afford credit in recent years. Although interest payments on debt rose substantially, the share of interest in state–local budget outlays—about 3.5 percent of the total—in 1970 remained unchanged from 1965. Moreover, total debt declined significantly in

relation to state-local own-source revenues, and remained about the same in relation to personal income.[8]

Capital Outlays and Debt Financing

Capital outlays in the past decade, although steadily rising, did not experience rates of growth as high as those for current operations. As a result, capital spending dropped from 25 percent of all outlays in 1960 to 20 percent in 1970. Capital outlays rose from around $15 billion in 1960 to almost $30 billion by 1970, representing average annual gains of 7.0 percent, well below the 9.7 percent increase in total spending.

Question may appropriately be raised as to whether credit market conditions and their effect on bond sales served to hold capital spending in fiscal 1970 (the benchmark year of these projections) below levels it would have reached in the absence of those strictures. There is little indication that this was actually the case. The Federal Reserve Board study, discussed above, found that the effects of the $5.2 billion shortfall in bond sales during fiscal 1970 on original plans for capital spending were relatively slight. An estimated $1.6 billion in planned capital outlays remained suspended at the end of fiscal 1970 largely as a result of the credit crunch; however, because of lags involved in capital spending, the cutback would be stretched out over time; only a small portion affected actual capital outlays in 1970. The effect on capital spending was minimal mainly because states and localities raised 60 percent of the

8. Historical data appear in Table 9.4, along with the projections.

Table 9.3

Debt Transactions of State-Local Governments

Actual and Projected, Selected Fiscal Years, 1950–1980[a] (Millions)

Period	Total debt outstanding	Long-term debt			Net long-term debt[d]
		Outstanding	Issued[b]	Retired[c]	
Actual:					
1950	$ 24,115	$ 23,056	n.a.	n.a.	n.a.
1955	44,267	42,272	$ 7,221	$2,351	$ 38,502
1960	69,955	66,801	7,955	3,458	61,596
1965	99,512	94,204	11,249	5,040	85,942
1969	133,548	123,466	15,453	6,538	114,368
1970	143,570	131,415	12,848	7,011	121,733
Projected:					
1975	211,161	191,506	25,859	10,013	175,803
1980	310,046	282,891	34,745	14,999	259,694

a. Outstanding debt as of the end of the fiscal year.
b. Includes refunding issues.
c. Includes refinancing.
d. Total long-term debt less cash and securities held as debt offsets.
Source: Actual data from U.S. Department of Commerce, Bureau of the Census. Projections by Tax Foundation.

short-fall in long-term bond funds needed to finance these projects by short-term borrowing not subject to legal interest rate ceilings. Reductions in actual or planned liquid assets, according to the Federal Reserve Board study, were of secondary importance in financing capital projects, and the use of current revenues to substitute capital for current expenditures was inconsequential.

In the past decade as a whole, approximately one-half of state–local capital spending was financed by long-term borrowing. In recent years the portion has risen to around 60 percent, reflecting in part the changing mix of capital spending by function, especially the decline in the portion of total bond sales represented by roads and streets. Roads and streets still constitute the largest component of capital outlays. Only about 15 percent of these outlays, however, are financed by borrowing. Education, utilities (water, sewers, transit, etc.), and housing are the other major functions for which long-term borrowing is extensive.[9] In 1970 security issues for education were equal to 66 percent of capital outlays for education; for functions other than education and highways, bond proceeds exceeded capital outlays during the period. (As noted previously, actual outlays lag behind bond sales for a specific project because the work is spread out over time.)

Projections of Debt

It seems clear that future sales of state–local securities will be linked closely to capital outlays. While money and credit conditions have pronounced effects on the volume of offerings, these effects are likely to be short-lived.

Table 9.4

State–Local Debt in Relation to Revenue and Personal Income

Actual and Projected, Selected Fiscal Years, 1950–1980

Year	Debt as percent of: Own-source revenues[a]	Personal income
Actual:		
1950	119.2	10.6
1960	148.4	17.4
1965	145.9	18.5
1970	124.3	18.0
Projected:		
1975	112.2	18.1
1980	113.1	18.8

a. General revenues from own sources plus utility revenues.

Source: Actual data from U.S. Department of Commerce. Computations and projections by Tax Foundation.

Based on relationships in recent years, and projected capital outlays, long-term borrowing for new capital would rise from around $18 billion in fiscal 1970 to $26 billion in 1975 and $35 billion by 1980 (Table 9.2). The projections for 1975 depict a leveling in the volume of new security issues in the 1971–1975 period.

Based on these projections for security offerings, and other financial transactions,[10] total outstanding debt would rise from around $144 billion at the end of fiscal year 1970 to $310 billion by 1980 (Table 9.3). The rate of increase for the decade would be somewhat higher than in the sixties, but not nearly so high as that experienced during the

9. Many of these "other" bond issues are for multiple-purpose projects. For monthly and annual data on the use of proceeds of new security issues, see *Federal Reserve Bulletin*, monthly issues.
10. See Appendix I for assumptions and methodology.

fifties. As projected, total debt would continue to decline in relation to own-source state-local revenues (and even more sharply in relation to total revenues, including Federal grants-in-aid), and would remain in the vicinity of 18 percent of personal income, the same as in 1970 (Table 9.4).

Other Financial Considerations

The projected levels of debt financing appear to be well within the borrowing capacity of states and localities, on the basis of their expected future revenues. Before judging the over-all financial situation, account is taken of two other aspects of state-local operations: required holdings of cash and securities, and claims on general receipts outside the general accounts.

Cash and Security Holdings

State and local governments typically hold large sums in the form of liquid assets—cash and securities—as offsets to long-term debt; as bond funds pending the completion of construction or capital projects; and as day-to-day working capital. In total, these funds (exclusive of insurance trust systems) rose from $29 billion in 1960 to $64 billion in 1970, and tended to average around 44 percent of outstanding debt.

The projected levels of these financial asset holdings by type, along with historical data, are presented in Table 9.5. The indications are that cash and security holdings, excluding insurance trust systems, would rise further to around $100 billion in 1975 and $145 billion in 1980.

Other Operations

Some other transactions of governments do not enter directly into Bureau of the Census tabulations of general

Table 9.5

Cash and Security Holdings of State-Local Governments, by Purpose—excluding Insurance Trust Systems

Actual and Projected, 1960-1980[a]
(Millions)

Fiscal year	Total holdings	Purpose		
		Long-term debt offset	Bond funds	All other
Actual:				
1960	$ 29,313	$ 5,203	$ 5,892	$18,216
1965	43,821	8,261	9,764	25,795
1970	63,517	9,682	13,251	40,585
Projected:				
1975	99,767	15,703	24,152	59,912
1980	145,261	23,197	32,452	89,612

a. End of fiscal years.
Source: Actual data from U.S. Department of Commerce, Bureau of the Census. Projections by Tax Foundation.

expenditures, but occasionally augment or draw upon funds derived from general revenues or borrowing. In particular, there are typically deficits in the operation of some utility systems (notably water and transit services), profits on monopoly liquor stores operated in 17 states and a few localities, and government contributions to employee retirement systems made to their own systems on behalf of their own employees. Projected requirements for these purposes are included in the over-all summary table.

Summary of Over-All Finance

Table 9.6 summarizes the projections of the elements entering into the sources and uses of major state–local general funds. The results indicate potential surpluses on the over-all accounts of around $13 billion in 1975 and $6 billion in 1980.

The study has not attempted to project the year-by-year course of state–local finance, but has singled out the years 1975 and 1980 for analysis. The answers derived, however, can be construed as representative of the seventies generally. As of 1972 a number of states

Table 9.6

Summary of Source and Use of Major State–Local Government Funds[a]

Actual and Projected, Selected Fiscal Years, 1965–1980
(Millions)

Source or use	Actual			Projected	
	1965	1969	1970	1975	1980
Source of funds:					
General revenue	$74,000	$114,550	$130,756	$227,632	$329,011
Profit on liquor stores	275	405	389	499	609
New long-term security issues	11,249	15,453	12,848	25,859	34,745
Other borrowing[b]	1,081	3,475	4,185	1,500	1,500
Total funds available	86,605	133,883	148,178	255,490	365,865
Use of funds:					
General expenditures	74,546	116,728	131,332	214,800	320,021
Long-term debt retired	5,040	6,538	7,011	10,013	14,999
Employee retirement	1,794	2,854	3,296	6,065	11,160
Deficit on utility operations	978	1,385	1,212	2,299	3,784
Additions to liquid assets	4,549	5,394	3,680	9,692	10,353
Total funds required	86,907	132,899	146,531	242,869	360,317
Funds available less funds required	−302	+984	+1,647	+12,621	+5,548

a. Excludes receipts, expenditures, and liquid assets of social insurance systems; utility and liquor store operations are entered on a net basis. Also excludes some interfund and other transactions not detailed separately in Bureau of the Census reports.

b. Net increase in total debt outstanding minus the difference between long-term debt issued and retired.

Source: Actual data from U.S. Department of Commerce, Bureau of the Census. Projections by Tax Foundation.

and localities were already projecting surpluses in their fiscal 1973 budgets, even without the additional funds they were to receive in the first installment of Federal revenue sharing grants (see Appendix III).

The very anticipation of a financial condition in the future more favorable than has existed previously can trigger actions which will change the course of actual events. Among major options under discussion currently are: (1) a reduction in state or local taxes, especially property taxes; (2) paying off outstanding debt; (3) building up liquid assets to meet future spending needs; and (4) spending the "surplus" funds, either for current operations or for capital improvements.

Experience has shown that the problem of deciding how to dispose of an expected surplus can be more vexing than that of how to avoid a threatened deficit. A 1965 Tax Foundation study found that, while most states have established budgetary procedures for coping with anticipated deficits, few had made provision in advance for dealing with a surplus.[11]

Discussions today are faintly reminiscent of those which occurred during World War II, when economists, political scientists, and practitioners were debating the question: what should be done about the (state) surplus?[12] Clearly the actual course of events will depend upon the kinds of policy decisions which will be made as regards the disposition of surpluses.

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11. *State Expenditure Controls: An Evaluation*, Research Publication No. 3, 1965, pages 69–71.
12. Large and unexpected surpluses were built up during the War as a result of rapidly expanding tax revenues and restrictions on expenditures. The problem was discussed in *The General Fund Surplus Problem in California*, by Dorothy C. Thompkins, Bureau of Public Administration, University of California, Berkeley, 1943. An important difference between then and now was that tremendous backlogs of capital investment needs were developing then, the coming population explosion was not yet evident, and there was widespread concern about postwar unemployment. Then as now, there was concern over state–local fiscal policy as related to attempts to control inflation.

Appendix I
Assumptions, Methodology, and Background Tables

The broad assumptions underlying this study are spelled out in Chapter II. This Appendix section provides detail concerning projections of individual items.

Population

The projections of population used in this study are those of the Bureau of Census, U.S. Department of Commerce, Series C, as published in *Current Population Reports*, Series P-25, No. 470 (November 1971). Table A.1 shows the range of projections for 1975 and 1980 under alternative assumptions about fertility rates.

Education

Projections of the three functional categories of education were developed separately, further broken down into current operating and capital outlays.

Local Schools. Enrollment estimates (Table 3.5) are those of the Office of Education, U.S. Department of Health, Education, and Welfare, as published in *Projections of Educational Statistics to 1979–80*, 1970 edition. These estimates are based on Series C population projections of the Bureau of the Census. The Office of Education estimates generally assume a continuation of the 1959–69 trends in public school enrollment rates in relation to population for ages 5 and 6, and in the trends in retention rates for other grades. For nonpublic enrollments, the projections imply a decline of 300,000 from 1969 to 1972 for grades K-8, with stability thereafter; high school enrollments are held constant at the 1969 level. Total enrollments in nonpublic schools are estimated at 5.6 million in 1970, and at 5.4 million in 1975 and 1980.

Average daily attendance in public schools is assumed to continue to equal 92.6 percent of total enrollments.

Current expenditures per pupil in average daily attendance (Table 3.6) are projected in this study as rising, in constant dollars, at the same rate as in the period 1960–1970 (4.7 percent annually). Current dollar equivalents were calculated by adjusting the resulting data for the assumed rise in general prices (3.9

Table A.1

Alternative Projections of Total Population, 1975 and 1980[a]

Series	Number (millions)[b]		Percent increase		
			Annual rate		Total
	1975	1980	1970–1975	1975–1980	1970–1980
B	218.2	236.7	1.3	1.6	15.8
C	217.4	233.8	1.2	1.5	14.2
D	216.6	230.9	1.1	1.3	12.7
E	215.7	227.8	1.0	1.1	11.2

a. As of July 1. Includes armed forces abroad. The range of projections reflects primarily different assumptions concerning fertility rates.
b. Population as of July 1, 1970 estimated at 204.8 million.
Source: U.S. Department of Commerce, Bureau of the Census.

Table A.2

Recipient Rates under Public Assistance Programs

Actual and Projected, Selected Years, 1950–1980

Year	Total[a]	OAA	AFDC[b]	APTD[c]	AB	GA
	Number per 1,000 population in age group aided[d]					
Actual:						
1950	39.7	224.7	47.2	.7	.9	6.2
1955	35.1	174.7	39.3	2.5	.9	4.9
1960	39.3	138.4	47.6	3.7	.9	7.3
1965	40.1	114.9	62.4	5.3	.7	3.8
1969	54.8	106.5	103.4	7.1	.6	4.7
1970	67.5	103.3	138.6	8.1	.6	5.7
Projected:						
1975	86.1	93.1	201.8	11.0	.5	5.1
1980	90.7	84.8	216.2	13.9	.4	5.0

a. As of December. Totals may involve some overlapping among programs.
b. Prior to 1962 total could include as recipients the children and one parent as caretaker relative; beginning October 1962, eligibility was extended to both parents or one caretaker relative other than a parent.
c. Program initiated in October 1950.
d. Population age groups eligible for the several programs are generally: OAA—65 and over; AFDC—under 18; APTD—18 to 64; AB—18 and over; and GA—under 65.

Source: Basic data from U.S. Department of Health, Education, and Welfare. Recipient rates and projections by Tax Foundation.

percent annually, 1970–1975, and 3.0 percent annually, 1975–80). Total current operating outlays represent the number of students in average daily attendance multiplied by the projected current dollar costs per student.

Capital outlay projections are those of the U.S. Office of Education, adjusted to a current dollar basis on the assumption that the Associated General Contractors construction cost index will increase by 4.6 percent annually from 1970 to 1975, and 4.2 percent annually thereafter to 1980. The general assumptions of the Office of Education in their constant dollar projections are that: (a) the number of rooms constructed will follow the 1960–61 to 1969–70 trend, remaining constant at 70,000 rooms per year; and (b) that capital outlay per room in constant dollars will remain at $70,000 per room.

Higher Education. As with local schools, the enrollment estimates used in this study are those of the U.S. Office of Education (Table 3.10). The projections represent an extension of the trend of the past 11 years in the ratio of college enrollments (by sex, and by type and control of institution) to population aged 18 to 21 years. Full-time equivalents are based on the 1964 ratios of full-time to total enrollments by various categories of students and institutions, as determined in a special survey of the Office of Education.

Current expenditures per student, full-time equivalent, are projected by the Tax Foundation to increase at the rate of 2.5 percent annually in real terms, the same as experienced during the period from 1960 to 1970 (Table 3.11). Total current outlays for higher education represent the product of cost per full-time equivalent student and the number of students.

Capital outlay projections are those of the Office of Education, adjusted to the Bureau of Census data basis and for assumed changes in construction costs of 4.6 percent from 1970 to 1975 and 4.2 percent from 1975 to 1980. The U.S. Office of Education assumptions are that the cost of capital outlay per additional full-time equivalent student—over a five-year period—will remain constant at the 1967–68 level of $7,837 (in 1969–70 dollars).

Projections of current outlays for other education (state direct outlays for supervision of local schools, provision of state schools for the handicapped, etc.) assume constant absolute annual increments of $238 million in the seventies, equal to those of the last half of the sixties. This is a somewhat arbitrary technique, based generally on the assumption

Table A.3

Changes in Estimated Medicaid Costs (+) and Savings (—) under Social Security Amendments of 1972 (H.R.1)

(Millions)

Provision	Calendar year 1974
Changes in H.R. 1:	
Coverage of the disabled under Medicare	$ −70
Increase in Medicare Part B deductible from $50 to $60	+8
Reduction in Medicaid matching if States fail to perform required utilization review	−162
Imposition of premium, copayment and deductible requirements on Medicaid recipients	−89
Families with earnings under Medicaid: Eligibility extended 4 months	+33
Limitation on nursing home and intermediate care facility reimbursement to 105 percent of last year's payment	−22
Elimination of requirement that States move toward comprehensive Medicaid program by 1977	(a)
Elimination of requirement that States maintain their year to year fiscal efforts in Medicaid	−640
Payments to States under Medicaid for installation and operation of claims processing and information retrieval systems	+10
Increased Medicaid matching for Puerto Rico and the Virgin Islands	+10
More specific requirements as to eligibility for skilled nursing level of care	−14
100 percent reimbursement for the cost of certifying skilled nursing homes under Medicaid	+10
Expansion of Medicaid coverage to include inpatient care for mentally ill children	+120
90 percent Federal funding of family planning services	+36
Coverage of persons needing renal dialysis or transplantation under Medicare	−20
Preserving Medicaid eligibility for social security beneficiaries	
Total estimated reduction in Medicaid costs under H.R. 1	−790

a. The current law estimates take no account of the effect of the requirement that states move toward comprehensive Medicaid programs by 1977; therefore, no savings are attributed to the repeal of this requirement.

Source: U.S. Department of Health, Education, and Welfare.

that the relative rate of growth experienced in this period (over 30 percent annually) was associated with conditions not likely to exert the same force over a sustained period. No adjustment is made for differential price assumptions. For capital outlays, the same procedure of projecting absolute annual increases ($24 million) at the same rate as in the 1965–70 period was used, with additional adjustment for assumed future increases in the construction cost index.

Public Welfare

Cash Payments. The growth in cash aid is projected proportionately to growth in the number of persons assisted and the rise in payments per recipient. The number of recipients is generally based on a linear extrapolation of recipients in relation to eligible age categories during the sixties, with modifications for two categories. (See Table A.2.) It is assumed that the rise in the recipient rate (number of recipients per 1,000 eligible population members) for the AFDC category will gradually slow from recent experience. The other exception is in the general assistance category, where there is no pronounced long-term trend, but which is cyclically sensitive; the projected rate for general assistance is the average rate prevailing during the entire period of the sixties (5.1 per 1,000 persons under 65 years of age). Increases in cash aid per recipient in each category are projected at the same annual rates as experienced in the period from 1960 to 1970, as follows: OAA, 2.8 percent; AB, 4.5 percent; AFDC, 5.7 percent; APTD, 5.6 percent; and GA, 8.8 percent. Money payments (Table 4.2) for each category represent the product of the number of recipients and average payment per recipient. No adjustment was made in the projections to reflect Federal legislation in 1972, under which the Federal government will assume basic responsibility for providing living allowances for the adult categories (the aged, blind, and disabled). Similarly, the projections do not reflect potential savings in medical welfare costs under the law. (See Tables A.3 and A.4.)

Medical Vendor Payments. The projections assume that these payments in 1975 and 1980 will be a function of the 1969 level of payments, the index of growth in recipients, and the index of medical care prices. The index of recipient growth is estimated at 167.3 in 1975 (1969 = 100) and 189.6 in 1980; the medical care price index at 135.5 and 168.8 in 1975 and 1980 respectively. (See health and hospitals.)

Other Public Welfare. This category includes payments for institutional services in intermediate care facilities for persons not requiring skilled nursing home services, social services, administration, employee training, and other services. The projections assume that expenditures for these services will rise proportionately to recipients and average annual salaries of state–local employees.

Health and Hospitals

Expenditures for health are projected on the basis of the trend of the last half of the sixties, rather than the entire period, in view of recent developments which seem likely to continue in the seventies. In constant dollars, the projected rate of increase is 10.5 percent annually throughout the seventies. The data are converted to a current dollar basis by application of price changes averaging 5.4 percent from 1970 to 1975 and 4.5 percent thereafter to 1980. (These price effects reflect a 1.5 percent increase above the rise in the consumer price index generally, a differential based on experience in the period from 1965 to 1970.)

Expenditures for hospitals are projected to rise from 1975 to 1980 at the same rate experienced in the first four years following the introduction of Medicaid and Medicare; i.e., 12 percent annually. This rate has been remarkably steady in recent years, and there seems little basis for assuming a change; in the period from 1975 to 1980 the annual increase is dropped to 10 percent, assuming a slow-down in price increases.

Table A.4

Calendar Year 1974 Federal Costs of Supplemental Security Income for the Aged, Blind, and Disabled, and Child Welfare Services[a]

(Billions)

Program	Gross costs	Current law	Amount of increase
Aged, blind, and disabled:			
Benefit payments	$3.5	$2.1	$1.4
Savings clause for State supplementation	.3		.3
Food programs		.3	−.3
Administrative costs	.4	.2	.2
Subtotal, aged, blind, and disabled	4.2	2.6	1.6
Child welfare services	.2	(b)	.2
Total	4.4	2.6	1.8

a. As enacted in Social Security Amendments of 1972 (H.R. 1).
b. Current law cost is $46 million.
Source: U.S. Department of Health, Education, and Welfare.

Highways

Projections for current operations and capital outlays were developed separately, utilizing information published by the Federal Highway Administration, with data adjusted to a Bureau of the Census basis.

Current Operations. The major components of current operations are maintenance, administration, and research. The projections assume a continuation of the annual rate of increase experienced during the period from 1960 to 1970, adjusted for the rise in maintenance costs, or 2.3 percent annually in real terms. It is assumed that the maintenance cost index will be representative of other components of current operations, and that the index will continue to rise at a rate 1.5 percent in excess of the consumer price index, or by 5.4 percent annually from 1970 to 1975 and by 4.5 percent annually from 1975 to 1980. To arrive at current-dollar projections, these price changes (totaling 45 percent in the first half of the seventies and 39 percent in the latter half) are applied to the constant-dollar estimates.

Capital Outlays. Capital expenditures are projected to rise by around $800 million annually from 1970 to 1975, and by $730 million annually in the latter half of the seventies. The percentage rates are 6.3 and 4.5 respectively, for the two periods, as compared with an annual rate of 5.4 percent in the sixties as a whole. These rates of change are somewhat arbitrary; they take account of higher authorizations recently enacted for Federal grants, future growth in Federal Highway Trust Fund revenues and in state–local highway-user receipts; and assume a narrowing in the gap between Federal authorizations and disbursements. In fiscal years 1969 and 1970 combined, total Congressional authorizations for highway expenditure were $10.4 billion, of which only

Table A.5

Employment and Payrolls of State-Local Governments[a]

Actual and Projected, Selected Calendar Years, 1950–1980

Calendar year	Number of full-time equivalent employees		Wages and salaries (millions)	
	Total	Education	Total	Education
	Number or amount			
Actual:				
1950	3,722	1,536	$ 10,368	$ 4,292
1955	4,443	1,915	15,992	6,909
1960	5,530	2,494	25,162	11,852
1965	6,849	3,289	38,463	19,230
1970	8,501	4,226	66,463	34,398
Projected:				
1975	9,726	4,639	103,246	51,354
1980	11,056	5,028	160,227	76,124
	Percent increase, selected intervals			
1950–1955	19.4	24.7	54.2	61.0
1955–1960	24.5	30.2	57.3	71.5
1960–1965	23.9	31.9	52.9	62.3
1965–1970	24.1	28.5	72.8	78.9
1970–1975	14.4	9.8	55.3	49.3
1975–1980	13.7	8.4	55.2	48.2
1960–1970	53.7	69.4	164.1	190.2
1970–1980	30.1	19.0	141.1	121.3

a. Includes all functions—general and other.

Source: Basic data from U S. Department of Commerce, Bureau of Economic Analysis. Computations and projections by Tax Foundation.

$8.6 billion was actually disbursed. The slower rate of growth assumed in the latter half of the seventies implies a slowdown in the rate of increase with the completion of the Interstate System. No account is taken of construction cost trends, since funding depends largely on financial arrangements, and, as shown in the text discussion, inflation has generally had the effect of reducing the physical volume of work done, rather than raising the dollars spent.

Other Expenditures

Expenditures for other general functions (Table 7.2) are generally based on the assumption that real per capita rates of increase will parallel those of the period from 1960 to 1970, and that prices will rise by 3.9 percent annually, 1970–1975, and by 3.0 percent annually, 1975–1980. An exception to this general treatment was made in the case of sanitation and sewerage; in that case projections derived by the foregoing method were adjusted upward by $3.5 billion and $4.0 billion in 1975 and 1980, respectively, reflecting the spread-out effects of added spending generated by Federal grants under the "clean-water" law enacted in 1972.

Projections of employment in education are based on estimates prepared by the Office of Education, U.S. Department of Education, published in *Projections of Educational Statistics to 1979–80.* (See Table A.5.) For all other functions, it is assumed that the percentage increase in employment will be equal to that from 1960 to 1970. Average wages are estimated to rise at the same rate experienced during the same period (5.5 percent annually), with an added factor of 9 percent annually to allow for higher inflation in the seventies than in the sixties generally.

Capital outlays for education and highways are projected as described above. These are the largest categories of capital spending. For all other functions, capital expenditures in the years 1965–1969 constituted around 15 percent of outlays for all purposes. The projections assume that this same relationship will hold in 1975 and 1980. (See Table A.6.)

Revenue Projections

Projections of tax receipts (Table 8.7) are based on the tax structure in effect in fiscal 1970, adjusted for new state tax enactments through October 1971 (the latter totaling $4.4 billion). No adjustment is made for an additional $1.6 billion in higher state taxes enacted later in 1971 and in 1972. (See Tax Foundation's *Tax Review*, March and September 1972.) Yields for each tax are projected according to the income elasticities shown in Table 8.6.

Tables A.7 and A.8 provide some perspectives on the response of the property tax to economic change.

Revenues from current charges and fees are projected as a function of expenditures for associated functions, with the share of charges and fees in relation to total expenditures following the trend pattern of the sixties generally (see Table 8.9).

The projections of Federal grants-in-aid for purposes other than general revenue sharing and municipal waste treatment assume that grants will remain at the same share of spending for each of the major state–local functions as they represented in fiscal year 1971. These relationships were as follows:

Function	*Percent financed by Federal grants*
Education	11.4
Highways	27.6
Public welfare	53.6
Health and hospitals	7.1
Housing and urban development	63.1
Other	8.6

In other words, the assumption is that Federal aid for these functions will grow commensurately with expenditures as projected independently. The total of grants thus derived was then adjusted upward to take account of general revenue-sharing and the "clean-water" law enacted in 1972. It is assumed that general revenue-sharing grants will amount to $6.2 billion in 1975, as presently legislated; and that Congress will act to continue these grants at the level of $6.4 billion in fiscal 1980. The projections imply that Federal grants under the new "clean-water" law will be spaced out over a period of years, and will total $3.5 billion in fiscal 1975 and $4.0 billion in 1980.

Table A.6

Capital Outlay of State–Local Governments for All Functions

Actual and Projected, Selected Fiscal Years, 1955–1980

Fiscal year	Capital outlay		
	Total	General	Utility
	Amount (millions)		
Actual:			
1955	$10,706	$ 9,544	$1,162
1960	15,104	13,697	1,407
1965	20,535	18,345	2,190
1970	29,650	27,214	2,437
Projected:			
1975	43,099	40,002	3,097
1980	57,909	53,889	4,020
	Percent increase, selected intervals		
1955–1960	41.1	43.5	21.1
1960–1965	36.0	33.9	55.7
1965–1970	44.4	48.3	11.3
1970–1975	45.4	47.0	27.1
1975–1980	34.4	34.8	29.8
1960–1970	96.3	98.7	73.2
1970–1980	95.3	98.1	65.0

Source: Basic data from U.S. Department of Commerce, Bureau of the Census. Computations and projections by Tax Foundation.

Over-All Finance

Table A.9 presents data on the state-local surplus or deficit on a national income accounts basis for calendar periods from 1960 to 1972.

New security issues (Table 9.2) are projected on the assumption that borrowing will finance 60 percent of capital outlays, about the same as in three of the four latest years reported, but higher than the average of around 50 percent earlier in the sixties. The shift reflects the relatively lower expected weight of highway issues in the total for the seventies. Whereas only about 15 percent of highway capital outlay was financed by state–local borrowing in recent years, well over two-thirds of capital spending for other functions was financed by bond proceeds.

The amount of debt retired annually is

Table A.7

Selected Measures Relating to the Economic Base of the Property Tax in the Postwar Period

(Billions)

Measure	1945	1956	1958	1961	1966
Gross national product	$211.9	$ 419.2	$ 447.3	$ 520.1	$ 749.9
Privately owned national wealth:					
Land and structures	318.4	795.1	885.8	1,064.9	1,446.0
Realty plus producers durables and inventories	414.8	1,099.1	1,201.6	1,428.9	1,941.8
Gross assessed value of property subject to local general property taxes	n.a.	258.0	n.a.	339.5	457.4
Gross assessed value of real property subject to local general property taxes	209.8	209.8	n.a.	281.9	393.2
Estimated market value of locally assessed real property	n.a.	700.0	n.a.	969.0	1,277.0
Property tax revenue[a]	5.0	12.9	15.0	19.1	26.3

a. Data apply to the fiscal year ending six months following the calendar year indicated in column headings.

Source: Adapted and updated from material in Dick Netzer, *Economics of the Property Tax*, The Brookings Institution, Washington, D.C. 1966, p. 190. Data on national wealth are from Raymond W. Goldsmith, *The National Wealth of the United States in the Postwar Period*, National Bureau of Economic Research, 1962; and *Statistical Abstract of the United States*, 1971, p. 328, originally published in U.S. Congress, *Institutional Investor Study Report of the Securities and Exchange Commission Supplementary Volume I, House Document* 92-64, Part 6, March 10, 1971. All other data are from periodicals published by the U.S. Department of Commerce—Bureau of the Census, and Bureau of Economic Affairs.

assumed to be 5.7 percent of long-term debt outstanding in each previous year, according to recent practices. Projected long-term debt equals debt at the end of fiscal 1970 plus new security issues minus debt retired in succeeding years to 1975 and 1980. Short-term debt is projected as rising by $1.5 billion a year, according to the 1966–1970 trend. Total debt outstanding is the sum of computed figures for long-term and short-term debt outstanding. (See Table 9.3.)

Table A.10 portrays historical changes in the composition of state–local debt.

Table A.11 compares yields on state–local bonds with those on other securities, 1960–1972.

Cash and security holdings (Table 9.5) in 1975 and 1980 are estimated separately according to purpose. Long-term debt offsets are projected at 8.2 percent of long-term debt outstanding, the same as in the 1966–1970 average. It is assumed that bond funds will amount to 93.4 percent of new security issues in the previous fiscal period, as was the case in the last half of the sixties. "All other" cash and security holdings are projected at 3.3 times short-term debt outstanding in 1975 and 1980, the ratio which prevailed in 1970.

Projections of other sources and uses of funds shown in Table 9.6 are based largely on recent experience. Profits on liquor stores are increased linearly according to the 1965–1970 trend. Deficits on utility operations are estimated by separate projections of revenues and expenditures at the rates of change experienced from 1960 to 1970, adjusted for price factors. State–local contributions to employee retirement funds (excluding those paid from general funds which are already covered in general expenditures) are estimated to rise at the rate of 13 percent annually, repeating the experience of the last half of the sixties.

Table A.8

Changes in Property Tax Revenues in Comparison with Selected Measures of Income and Wealth

Measure	Average annual percent increase		
	1956–61	1961–66	1956–66
Gross national product	4.4	7.6	6.0
Privately owned national wealth:			
Land and structures	6.0	6.3	6.2
Realty plus producer durables and inventories	5.4	6.3	5.9
Gross assessed value of property subject to local general property taxes	5.6	6.1	5.9
Gross assessed value of real property subject to local general property taxes	6.1	6.9	6.5
Estimated market value of locally assessed real property	6.7	5.7	6.2
Property tax revenue	8.2	6.6	7.4

Source: Computed from data in Table A.7.

Table A.9

State–Local Surplus or Deficit on National Income Accounts

Calendar Years, 1960–1972
(Millions)

Calendar year	Over-all surplus or deficit(−)	Surplus, social insurance funds	Surplus or deficit(−) general funds[a]
1960	$ 220	$2,146	$−1,926
1961	−522	2,291	−2,813
1962	936	2,516	−1,580
1963	1,186	2,772	−1,586
1964	1,676	3,092	−1,416
1965	962	3,387	−2,425
1966	1,266	3,728	−2,462
1967	−1,533	4,370	−5,923
1968	−346	4,975	−5,321
1969	686	5,698	−5,012
1970	2,815	6,518	−3,703
1971	4,794	7,538	−2,743
1972, by quarters[b]			
I	7,100	n.a.	n.a.
II	14,800	n.a.	n.a.

a. Excluding social insurance funds.
b. Seasonally adjusted annual rate.
Source: U.S. Department of Commerce, Bureau of Economic Analysis.

Table A.10

Gross Outstanding Debt of State–Local Governments by Type[a]

Selected Periods, 1950–1970

Year	Total debt outstanding	Long-term			Short-term
		Total	Full faith and credit	Non-guaranteed	
	Amount (millions)				
1950	$ 24,115	$ 23,056	$19,779	$ 3,275	$ 1,060
1955	44,267	42,272	30,539	11,733	1,995
1960	69,955	66,801	41,650	25,151	3,154
1965	99,512	94,204	56,417	37,786	5,309
1970	143,570	131,415	75,337	56,078	12,155
	Percent of total				
1950	100.0	95.6	82.0	13.6	4.4
1955	100.0	95.5	69.0	26.5	4.5
1960	100.0	95.5	59.5	36.0	4.5
1965	100.0	94.7	56.7	38.0	5.3
1970	100.0	91.5	52.5	39.1	8.5

a. Data represent debt for all functions—general and nongeneral.
b. End of fiscal years.
Source: Basic data from U.S. Department of Commerce, Bureau of the Census. Computations by Tax Foundation.

Appendix II

Text of Treasury Department Fact Sheet on Allocations under the Revenue-Sharing Act

Allocations

The $30.2 billion State and Local Fiscal Assistance Act of 1972, more commonly known as Revenue Sharing, will provide much-needed funds to States and local governments heavily burdened with high income and property taxes. The first checks will be mailed as soon as practicable to more than 38,000 States and communities throughout the United States. Interim regulations, designed to provide immediate guidance to States and local governments, will be published to fulfill the requirements of the Act as passed by the House and Senate.

Approximately half of the 1972 payment of $5.3 billion will be disbursed this Fall. The remaining portion of the 1972 entitlement will be mailed early in January 1973.

This amount will be increased by annual increments for each of the four succeeding years. The life of the Act runs five years beginning January 1, 1972. A total of $5.64 billion will be paid in fiscal year 1973 in addition to the $2.6 billion mentioned above; $6.05 billion in fiscal year 1974; $6.20 billion in fiscal 1975; $6.35 billion in fiscal year 1976 and $3.325 billion for July-December 1976.

The funds will be obtained from individual Federal income taxes and will be held in a special Revenue Sharing Trust Fund in the Department of the Treasury.

Data

A special study is now being completed by the Census Bureau to update the data required under the law for determining allocations. The Revenue Sharing figures which have been published are simply estimates from other data, some of it dating back six years. The new study will bring the data up to 1971 figures. Consequently, the exact amount that each government unit will receive will vary from these initial estimates.

Qualifications

All general-purpose State and local governments, including counties, cities, townships, boroughs, and villages are qualified for entitlements.

Entitlements

The State government shall be entitled to receive one-third of the total amount allocated to that State. The remaining two-thirds of the State's allocation shall be divided among the units of local governments.

The money will be apportioned to counties, cities and towns using a formula based on population multiplied by the general tax effort factor, multiplied by the relative income bearing on the sum of the products determined for all such local governments within that State.

Indian tribes and Alaskan native villages which have recognized governing bodies performing substantial governmental functions will receive an allocation that is part of the county total. This special allocation is based on population of that tribe or village in relation to the county area.

Two Formulas Used

The Act allocates trust fund monies to States under one of two formulas. Computers have taken both formulas into account for each state and selected the highest amount.

One formula is a three-factor formula—the population of the State multiplied by the relative income factor of that State, multiplied by the general tax effort factor of the State as it bears to the sum of the products for all states on the ratio to $5,300,000,000.

The other is a five-factor formula which is based on general population, urban population, per capita income, State income tax collections, and the general tax effort of the State.

Limitations

Other entitlement items in the Act concern maximum and minimum limitations on the allocations to county and other local governments within each State. Restrictions which are placed on the allocations to country and local governments include:

The per capita grant to a unit of local government or county area must be greater than or equal to 20 percent of the State's per capita grant. This is determined by taking the sum of the two-thirds of the State aggregate amount divided by the State population which will give the per capita grant for the State.

The maximum limitation for any county area or local government in the State is 145% of the State per capita grant.

There is a $200 minimum payment. However, the first payment for January 1, 1972 to June 30, 1972 will be the minimal amount paid in two parts of $100 each, the first in the Fall and the second early in January, 1973. This will be the same in the payment of July-December 1976.

Other Qualification Requirements

The law gives discretion to communities on how they spend their monies, but the law requires expenditure and obligation reports.

These entitlement reports must be published in general circulation newspapers within the geographic areas of each State and local government. The reports must also be made available to all communications media within the geographic area. In this manner all citizens will be provided with information regarding the use of Revenue Sharing monies.

No Matching Funds

Revenue Sharing funds may not be used by the State or local governments as matching funds for any Federal program. These funds may not be used for education.

Appeals Possible

If a State or local government believes that it has not received equitable treatment, it can appeal to the Secretary of the Treasury who will establish procedures to resolve such problems. Every reasonable effort will be made to correct difficulties which are brought to the attention of the Office of Revenue Sharing.

One Formula Change

If a State, once it has received Revenue Sharing funds, wishes to tailor its allocation formula to local problem areas, it has the option under the bill to amend its allocations by action of the State government once during the five-year program.

If a State believes that it is desirable to grant a relatively large portion of the funds on the basis of need, it can do this by increasing the weight of population by relative income levels. Conversely, relatively more funds could be distributed on the basis of population weighted by tax effort if it is desired to place greater emphasis on taxes raised locally.

Trust Funds

States as well as local governments are required to place Revenue Sharing monies into trust funds and account for them separately from other funds. This rule was established so that the Secretary of the Treasury can make periodic compliance studies and Congress will be assisted later in determining whether the Revenue Sharing program should be continued, revised or terminated at the end of the five-year period.

The Secretary of the Treasury will report to the Congress not later than March 1 of each year on the operation and status of Revenue Sharing allocations during the previous year.

Normal Audit Procedures

In order to aid and assist in the audit procedures, each State and local government must use fiscal, accounting and audit procedures which conform to the guidelines established by the Secretary of the Treasury and Comptroller General. The guidelines will provide that in most situations the States and localities will be permitted to follow their normal accounting procedures.

Each governmental unit must provide to the Secretary and the Comptroller General of the United States on reasonable notice access to and the right to examine such books, documents, papers or records as they may reasonably require for purposes of reviewing compliance with this Act.

Anti-Discrimination

The law stipulates that no person shall on the ground of race, color, national origin or sex be excluded from participation in, be denied the benefits of, or be subjected to discrimination under a program or activity funded in whole or in part with Revenue Sharing funds.

Other Qualifications

In order to qualify for payments, each State or local government must, for each entitlement period beginning on or after July 1, 1973, establish in advance a number of matters to the satisfaction of the Secretary. These include the setting up of a trust fund; use of the amounts and interest during a reasonable period of time and the use of monies only for priority expenditures.

"Priority expenditures" mean:

(1) Ordinary and necessary maintenance and operating expenses for—

(a) Public Safety (including law enforcement, fire protection and building code enforcement).
(b) Environmental protection (including sewage disposal, sanitation and pollution abatement).
(c) Public transportation (including transit systems and streets and roads).
(d) Health.
(e) Recreation.
(f) Libraries.
(g) Social services for the poor or aged, and
(h) Financial administration; and

(2) Ordinary and necessary capital expenditures authorized by law. No unit or local government may use entitlement funds for non-priority expenditures which are defined as any expenditures other than those included in (1) and (2) above. The chief executive officer of each unit of local government must certify to the Secretary that entitlement funds received by it have been used only for priority expenditures as required by the Act.

Prevailing Wages

Prevailing wage rates are to be followed. Each governmental unit must agree that persons employed in jobs financed in whole or in part out of its trust fund are to be paid wages not lower than the prevailing rates of pay for persons employed by that government.

The penalty provisions in the Act contain authority to withhold payments if a State or local government fails to comply with provisions of the Act, has had reasonable time for a hearing and has not taken corrective action within a 60-day period. Money withheld by the Secretary of the Treasury will be transferred from the trust to the general fund.